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ABSTRACT

Intended for parents and legal guardians of mentally retarded persons, the manual provides guidelines for estate planning. An overview of definitions, causes, and prevalence factors in retardation is followed by reviews of the major financial assistance governmental programs such as Medicare, and Supplemental Security Income, and of legal requirements regarding private support by family members. Estate planning mechanisms are considered in four chapters on guardianships, estate and gift taxation, wills and administration of estates, and trusts. Legal requirements are noted as are recommended procedures and provisions. The concluding three chapters address tax issues with separate attention devoted to life insurance, annuities, and generation-skipping transfers. Sample will and trust provisions are appended along with a resource guide for further reading. (CL)

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ESTATE PLANNING FOR RETARDED PERSONS AND THEIR FAMILIES

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TABLE OF CONTENTS

CHAPTER Page

FOREWORD i

INTRODUCTION...................... iv

ONE SUPPORT OF THE RETARDED CHILD GOVERNMENT ASSISTANCE 1

TWO SUPPORT OF THE RETARDED CHILD FAMILY ASSISTANCE 15

THREE GUARDIANSHIPS 27

FOUR ESTATE PLANNING 47

FIVE WILLS & ADMINISTRATION OF ESTATES . . 67

SIX TRUSTS 81

SEVEN LIFE INSURANCE...................... 115

EIGHT ANNUITIES 121

NINE GENERATION-SKIPPING TRANSFERS 137

APPENDIX A - SAMPLE TRUST PROVISIONS 147

APPENDIX B - RESOURCE GUIDE FOR FURTHER READING 150

FOREWORD

The materials in this text are designed to serve as a guide to parents, guardians, and their legal counsel on the legal issues peculiar to estate planning for retarded citizens and their families. Much of the discussion, however, is applicable to persons having other handicaps or illnesses which limit their ability to care for themselves independently of others.

The text begins with an Introduction entitled "Overview of Mental Retardation" which was prepared by Dr. James Mann, Director, Research and Training Center for the Handicapped and Professor of Special Education and Clinical Psychiatry and Human Behavior, University of Mississippi. The authors wish to thank Dr. Mann for making an invaluable contribution to the content of this book.

The special considerations and issues concerning financial care of retarded persons provide the major focal point for this text. These issues are specifically covered in the chapters on "Support of the Retarded Child- Government Assistance" and "Support of the Retarded Child-Family Assistance." Included is an overview of the major government programs offering financial assistance, with emphasis on asset and income limitations to qualification for such benefits. Complex questions concerning the extent of legal obligations of support owed by parents to their retarded children and the attachment of assets of retarded persons and their parents by providers of services also are treated in these chapters. The remainder of the text discusses the relationship of these issues to other matters such as drafting of wills, creation of trusts, and establishment of guardianships.

Three chapters are devoted to several mechanisms which can be utilized in planning the estates of retarded persons and their families— "Guardianships", "Wills" and "Trusts". Legal requirements necessary to establishment of such relationships or valid execution of needed documents are considered along with the purposes which these mechanisms can be expected to serve. Particular procedures and provisions for retarded persons are recommended as being appropriate for use in this area of estate planning.

Tax issues and methods of creating an estate complete the material. The chapter on *Estate and Gift Taxation* provides an overview of the principles of estate and gift taxation, including revisions enacted under the Economic Recovery Tax Act of 1981. Separate treatment is given the *Generation-Skipping Transfer Tax*, due to its application to certain transfers in trust. Finally, *Life Insurance* and *Annuities* are described from the standpoint of their usefulness as a major source of funds for trusts created for a retarded person.

Since each individual has a unique personal situation, professional advice is needed on an individual basis to determine the applicability of the principles discussed in this text. This book, therefore, is a guide to serve as a compilation of the legal issues involved and the alternatives available in planning the estates of retarded citizens and their families.

Without support and encouragement from many persons, this project for the particular benefit of Mississippians would not have been initiated or completed. The authors would especially like to acknowledge the constant interest and help provided by the late C. M. Scott, a former President of the Lafayette County Association for Retarded Citizens, to whom the book is dedicated, and the Lafayette County Association for Retarded Citizens which provided the impetus for the project and spearheaded the effort to obtain funding. Dr. H. Rutherford Turnbull, III, Chairman of the Department of Special Education, University of Kansas, and Mr. Melvin D. Heckt, Attorney at Law, Minneapolis, Minnesota, both read the original manuscript and offered many helpful suggestions for improving the final text. Dr. Jan Duker, Executive Director, Department of Mental Health, State of Mississippi; Dr. Ansley Bacon-Prue, Director, Mississippi University Affiliated Programs; and Mrs. Carla Hopkins, former President, Lafayette County Association for Retarded Citizens supported the project throughout and were instrumental in each phase of development.

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October, 1981

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INTRODUCTION

OVERVIEW OF MENTAL RETARDATION

Definitions

There is no single definition of mental retardation that receives unanimous endorsement. However, the definition offered by the American Association on Mental Deficiency (Grossman 1973; revised 1977) is generally accepted among professionals in the field of mental retardation. It currently reads, "Mental Retardation refers to significantly subaverage general intellectual functioning existing concurrently with deficits in adaptive behavior and manifested during the development period."[1]

This definition contains psychometric and social inadequacy elements and specifies an upper chronological age for the emergence of this condition. All three criteria have to be met before an individual could be classified as mentally retarded. Mental retardation is not a single disease, syndrome, or symptom; it is a state of impairment, recognized in the behavior of the individual, and its causes are many.

The American Association on Mental Deficiency's manual on terminology and classification in mental retardation (1977) listed how these factors are to be measured:

(1) Significantly subaverage general intellectual functioning—The factor is defined as performance on an individual test of intelligence of greater than two standard deviations below the population mean.

(2) Originates during the developmental period—This criterion was put into operation by setting eighteen years as the approximate upper chronological age for the developmental period.

(3) Impairment in adaptive behavior—This emphasis on "deficits in adaptive behavior" makes it clear that mental retardation is a product of the interaction between an individual's capabilities and the enrionmental demands. It is defined as the effectiveness or degree with which an individual meets the standards of personal independence and social responsibility expected for his/her age and cultural group. Since these expectations of adaptive behavior vary for different age groups, deficits in adaptive behavior will vary at different ages. These may be reflected in the following areas:

During infancy and early childhood in:

1. Sensory-motor skills development
2. Communication skills (including speech and language)
3. Self-help skills
4. Socialization (development of ability to interact with others)

During childhood and early adolescence in:

5. Application of basic academic skills in daily life activities
6. Application of appropriate reasoning and judgment in mastery of the environment
7. Social skills (participation in group activities and interpersonal relationships)

During late adolescence and adult life in:

8. Vocational and social responsibilities and performance.[2]

To be classified as mentally retarded, the individual must be clearly deficient in adaptive behavior. There are many persons whose IQ's are below 70 but who are adequate in their jobs or in their schools; therefore, such persons would not be labeled mentally retarded.

The diagnosis of mental retardation is made on the basis of "present" level of functioning, and with no reference to prognosis for the individual's future status. A person may be "cured" of mental retardation by improving his intellectual functioning or by changes in the expectations of society. For example, environmental consideration of this criterion of mental retardation could result in an adult with a very low IQ who may function quite adequately living the life of an employee on a small Delta farm. This same individual might be unable to function independently in a large city such as Memphis. He may be considered retarded if he lived in Memphis and nonretarded on the Delta farm.

No attempt is made to differentiate mental retardation from other disorders of childhood associated with impaired intellectual performance, such as autism or brain damage. Mental retardation is a general term that applies to a diverse group of people with varied causes which have the common effect of lowering an individual's level of intellectual functioning and adaptive behavior. In borderline cases, the line between the mentally retarded and nonretarded becomes increasingly nebulous. Adequate measures of adaptive behavior are lacking, and its measurement is quite subjective at this time.

The American Association on Mental Deficiency divides the degree or levels of mental retardation into four categories: "mild," "moderate," "severe," and "profound," based on the degree of deviation from an average person's adaptive behavior and measured intelligence.[3] Under this system, the levels of mental retardation vary from extreme impairment to rather minor impairment.

It is estimated that 75% of all retarded Americans are only "mildly so." On IQ tests—which at best are very rough measures of certain kinds of intelligence—mildly retarded people score approximately 55-69.[4] If given appropriate educational opportunities, with special education teachers, they can be taught reading and writing, social and vocational skills, and can earn their living in simple jobs. They may marry, and they may have normal children. Mildly retarded persons typically achieve economic self- sufficiency.

It is important to note that the majority of mildly retarded persons live and work independently in the community, often needing only minor assistance. Typically, as children, they have been unable to cope with reading, writing, and arithmetic, but in all other areas they may be quite normal. Once these individuals leave school and enter the labor market, mildly retarded persons usually blend into the labor force and pass into normality.

About 20% of retarded persons are "moderately" retarded, with an approximate IQ range of 40-54.[5] While they cannot go much beyond second grade in academic subjects, they can be trained in manual skills. They can hold jobs; however, they need living arrangements that give them some supervision. This group can be productive in sheltered workshops. Some of these persons might be able to handle small sums of money but be unable to deal with large sums. These persons, as children, typically attend special education classrooms in the public schools in Mississippi. As adults, more and more will be able to function relatively independently in the communities if Mississippi expands its community services for the retarded to include sheltered workshops, group homes, halfway houses, and other support services.

Probably about 5% of retarded citizens are either "severely" retarded with IQ's from 25-39 or "profoundly" retarded with IQ's below 25.[6] They require continuous care, although many of them can be taught to toilet, dress, and feed themselves. Members of the severely and profoundly handicapped group will have no concept of property or money.

It is obvious that no simple distinction between competent and incompetent individuals exists. There are degrees of competency ranging from full competency to complete incompetency among retarded persons. In addition, mental retardation professionals are well aware that there are usually intraindividual differences depending on specific tasks being evaluated. That is, a single retarded individual may be competent on some tasks but not on others.

Mississippi state laws do not recognize this reality. In many of the legal provisions of Mississippi, the mentally retarded are lumped with the mentally ill into a non compos mentis category, and persons so classified are equated with infants.[7] This term has an all-or-nothing implication that does not adequately reflect the range of functioning that mentally retarded persons possess. Living with an intellectual handicap does not usually mean incompetence. The large majority of retarded persons are able to make free and independent decisions.

Causes

The recent manual of the American Association on Mental Deficiency (Grossman, 1977) provides us with a framework for reviewing the etiological classifications. Mental retardation can be caused by or associated with infections and intoxicants (e.g., rubella or syphillis); trauma or physical agent (e.g., asphyxia and lead poisoning); metabolism, growth and nutrition (e.g., PKU and protein deficiency); chromosomal abnormality (e.g., Down's syndrome); gross postnatal brain disease; unknown prenatal influence; gestational disorders; retardation following psychiatric disorder; and environmental influences.[8]

In spite of biomedical progress in uncovering genetic conditions and toxic agents in the environment that may be linked to retardation, in the vast majority of cases of retardation nothing can be confidently pinpointed as the cause of the condition. The bulk of the retarded individuals are only mildly retarded, and the overwhelming majority of these cases have unknown causes.

The majority of the mildly retarded are cultural-familial retardates. Cultural-familial implies that the condition stems from a complex interaction of both environmental (cultural) and hereditary (familial) factors. While there is no definite proof, it is believed that the majority of cases are caused by early cultural and social inadequacies.

The known causes of mental retardation, for the most part, are found at the moderate, severe, and profound levels. For example, a condition almost always associated with moderate to severe retardation is Down's syndrome. A characteristic of Down's syndrome is the presence of extra chromosomal material in the human cell.

Prevalence

The President's Task Force on the Mentally Handicapped estimated the prevalence of mental retardation at about three percent; therefore, more than six million Americans will, at some time during their lives, be labeled mentally retarded.[9] This figure of 3% is accepted in most scientific writings. However, this 3% figure has been criticized by some researchers as being excessively high.[10] There is probably no reliable count of the number of mentally retarded persons as such because of the extreme difficulty of applying the label to many persons in the mildly retarded and borderline areas.

A great many environmental factors affect the prevalence of mental retardation. Among the more striking examples are the standards and practices of the community and factors related to age, socioeconomic status, ethnicity, sex, and geographical residence.[11]

For example, prevalence estimates of mental retardation show marked age variation. Surveys consistently show a peak during the school years and a sharp drop in adolescence. Mercer (1973) found the following rates in her case-finding surveys: age zero to four, 0.7 percent; ages five to nine, .54 percent; ages ten to fourteen, 1.15 percent; ages fifteen to nineteen, 1.61 percent; ages twenty to twenty-four, 0.90 percent; and ages above twenty-five, 0.13 percent.[12] The peak period of identification in Mississippi is during the early school years and represented 3.76 percent of the school population.[13] However, the peak period may vary from state to state.[14]

Most "temporarily" retarded persons are mildly retarded, and the vast majority of this group come from socioeconomically depressed backgrounds and have retardation that is not accompanied by physical signs. These individuals, diagnosed as mildly mentally retarded, often lose this label when they leave the school system. Failure as a student need not mean failure in later life. Thus the number of cases of mental retardation fluctuates. Mild mental retardation may pose a real problem in an academic setting; however, it may have little effect on an adult's performance in a job setting. Empirically, the school years consistently yield the greatest incidence of failure to meet the criteria of academic and social adequacy.

Developmental Disabilities

This is a current and very popular term that includes mental retardation. One federal statute (PL 95-602) defines developmental disability as a mental or physical disability that originated before the individual attained the age of twenty-two and includes any mental handicap which impairs the developmental growth of the child. This definition includes conditions such as mental retardation, cerebral palsy, epilepsy, and conditions associated with neurological damage.

The use of categorical labels was dropped (e.g., mental retardation) in defining persons with developmental disabilities. The statute focused instead on the actual barriers that stand in the way of normal development. The law states that any individual having substantial impairments in at least three of these seven functions of everyday living is in need of special service: self-care, receptive and expressive language, learning, mobility, self-direction, capacity for independent living and economic sufficiency.[15]

Developmental Model

Another concept that has influenced changes in services for mentally retarded persons is the developmental model. This developmental model has gradually replaced the deficit model because of a recognition that mentally retarded persons are capable of growth and learning regardless of their levels of retardation or age.[16]

The developmental model is based upon the assumption that all human beings are in a constant state of flux and growth. It further recognizes that although the general sequence of developmental stages is established, environmental variables can significantly alter the rate and direction of individual development and can enhance the mentally retarded person's ability to think rationally, act purposefully, and to deal effectively with his environment. Regardless of the degree of retardation, this model asserts that all persons have potential for growth and learning, and holds that there are only quantitative differences between a normal and a retarded person.

The Normalization Principle

The principle of normalization in relation to mental retardation was worked out by Wolfensberger and Nirje in the 1960's. Wolfensberger defined it as: "Utilization of means which are as culturally normative as possible, in order to establish and/or maintain personal behaviors and characteristics which are as culturally normative as possible."[17] Nirje defined this principle as: "making available to all mentally retarded people patterns of life and conditions of everyday life which are as close as possible to the regular circumstances and way of life of society."[18]

This principle of normalization has gained widespread acceptance in the field of mental retardation and has many implications. Normalization implies that the circumstances of everyday life should be as similar as possible for handicapped and nonhandicapped persons. Mentally retarded persons should live like nonretarded persons to the greatest extent possible.

Nirje (1969) pointed out that just as the normalization principle dictates that a handicapped child, like other children, should generally live at home, so should many handicapped adults live away from home because that is what is expected from nonhandicapped adults.[19]

Applying this principle to residential living has resulted in a move away from the placement of mentally retarded people in large institutions toward community centered forms of care; this process is often referred to as *deinstitutionalization*. Living in a community setting more closely approximates the normalization principle than living in a large, multi- purpose facility.

Successful implementation of these concepts depends, in part, upon availability and coordination of a wide range of residential and community services for mentally retarded persons. It involves more than the movement of mentally retarded persons from an institution to a community setting. These concepts can be easily undermined by inadequate planning and lack of financial support at the local level. In Mississippi, as elsewhere, the effort to apply these concepts have, in some instances, amounted to little more than the "dumping" of mentally handicapped adults from our institutions into unprepared communities.

Legal and Human Rights

Current major issues confronting the field of mental retardation concern the legal and human rights of the mentally retarded. Most professionals in the field of mental retardation would agree on two issues. First, a mentally retarded person can benefit at any point in his life and development from a program of education and training. Secondly, in line with the so-called normalization principle, the retarded person should live as nearly normal a life as possible.

One basic right that several class action suits have asked the court to confirm is the right to treatment when institutionalized.[20] Intensive services cannot completely undo the handicap of mental retardation; however, if started early, they can ameliorate it to a considerable degree. Moreover, treatment can and should keep institutionalized residents in good health and should help them develop what potential they have. For some severely retarded individuals, the least restrictive setting may be the institution. However, parents should not seek security for their handicapped children simply in the physical facility and personnel of the institution when it is an inappropriate placement.

Guardianship and Rights

Nowhere is the protection of rights more crucial to retarded persons than in guardianship. Total guardianship gives the guardian power to provide complete supervision over an individual, and certain legal rights of the person are totally removed.[21] Many retarded persons have no way of knowing their procedural rights in guardianship matters. Therefore, without counsel to protect their interests, they may find themselves held incompetent and stripped of their civil rights.

The National Association for Retarded Citizens took the position that "for a mildly retarded person and for some moderately retarded persons, the loss of all rights might be unthinkable unless there is a demonstrated need for protection which is substantially more important than the loss of such rights. On the other hand, the loss of rights for most profoundly and severely retarded persons may involve no real loss since they would not be exercising their rights, and their need for protection and supervision may be much more important for their welfare than retention of legal capacity."[22]

Since areas of competency can be quite varied, the President's Committee on Mental Retardation has recommended that the courts should consider each retarded person and determine guardianship needs on the basis of a comprehensive clinical evaluation. Recognizing that many retarded persons can learn to manage their own affairs, the Committee also recommended that the courts periodically review each case to see if grounds exist for modifying or terminating the guardianship.[23]

A guardian or conservator can make certain that the retarded person gets the kind of service which the community has a responsibility to provide. In an institution, the guardian or conservator can visit often, give gifts, provide entertainment, and emotional support. In the community, the retarded adult can be provided guidance in managing money, securing jobs, using transportation, and making use of leisure time.

Many parents of impaired children are quite willing and capable of looking after the interests of their child but have fears and misgivings about making provision for their child's future once the parents' health declines or they pass away. What is needed is to find parent successors who would continue to give compassionate, individual attention to a retarded child, and who would try to preserve the general type and quality of life that the child enjoyed when living with his/her parents.[24]

The Task Force on Law of the President's Panel on Mental Retardation recommended the following guidelines on this issue:

> But where legal guardianship of any kind is required, it should be carefully adapted to the specific requirements of the case. For some, of course, a comprehensive guardianship will be needed. But we urge that, as far as possible, mentally retarded adults be allowed freedom-even freedom to make their own mistakes. We suggest the development of limited guardianship of the adult person, with the scope of the guardianship specified in the judicial order. . . .Plenary guardianship should be reserved for those who are judicially determined to be incapable of undertaking routin day-to-day decisions and who are found to be incapable of basic self- management.[25]

Another august body, the American Association on Mental Deficiency, included the following prerequisites for guardianship appointments in its Policy Statement on Guardianship. The individual should:

1. be able and willing to perform the duties (of a guardian);

2. be able to maintain the best interests of the retarded ward as the paramount consideration in all decisions made on his or her behalf;

3. have no conflict of interest; individuals who have personal-financing interests in the ward or are professionally responsible for providing or supervising his or her care or treatment should not be appointed guardians under any circumstances; however, this consideration should not preclude appointment of parents, natural or adoptive, or other close family members where otherwise suitable;

4. be accessible-i.e., in close enough physical proximity and not be overburdened with other duties so that he or she is unable to interact regularly with his or her ward;

5. be in a position to serve as guardian over a reasonable period of years.[26]

The National Association for Retarded Children formulated its conclusion into six points which follow:

1. Guardianship is not necessarily the simple solution to the problem of what will happen after your death. Before seeking guardianship, you should be satisfied that there is a compelling reason which is in the best interest and welfare of your retarded son or daughter and that the advantages of guardianship clearly outweigh the disadvantages.

2. Guardianship, when used properly, may be of real assistance to your retarded son or daughter.

3. Guardianship, when used improperly, may result in a total denial of the rights of retarded persons, may impede their ability to make decisions for themselves which they can and should make, and may greatly dehumanize them.

4. Most parents are naturally concerned about protection for their children, but this form of security and protectorship can be secured in a number of ways without necessarily using the court-supervised formal guardianship.

5. Sometimes an effectively-drawn estate plan can eliminate the need for a legal guardian yet secure the same protection as a guardianship for your son or daughter.

6. Real security for your son or daughter lies in appropriate quality education, vocational rehabilitation training, financial assistance through SSI, medicaid, social security and other governmental benefits, appropriate quality residential living arrangements, state and federal legislation protecting the rights of retarded persons, and advocacy programs which reach out to monitor and secure services to provide for retarded citizens the quality of life that all citizens deserve.[27]

The bottom line is that if a person is seriously impaired in competency, there must be someone who will make wise and kind decisions for that person, if need be throughout his/her life. That someone must be willing to involve himself personally and individually. The retarded person must have viable, one-to-one support relationships.

Estate Planning and Rights

The greatest concern of most parents of mentally retarded persons is what will happen to their mentally retarded children after the parents have passed away. These concerns raise the issue of estate planning as parents seek ways to use what wealth they may have accumulated during their lives to benefit their retarded children after their death.

The National Association for Retarded Citizens took the position that in almost all cases, parents, grandparents, and other relatives should not permit their retarded son or daughter or relative to own or receive legal title to their money, property, or assets by will, inheritance, or gift, and should not make the retarded person the beneficiary of any life insurance policy for the following reasons:

1. Under the laws of most states, governmental agencies will take all but a very nominal amount of the assets owned by the retarded person or by the guardian of his estate for the cost of care and services provided by government to that person.

2. If a retarded person or the guardian of his estate owns assets in excess of a very little amount, he is disqualified from receiving certain important financial assistance benefits until the assets have been almost exhausted.

3. Many retarded persons are vulnerable to exploitation and are either totally incompetent to handle their own funds or incapable of managing more than their own earnings or nominal amounts of personal property or assets.

4. Court-supervised guardianship of the estates of retarded persons may result in more rigid financial management than the parents or relatives desire.

5. When a retarded person dies owning money or property, it will be distributed to his next of kin under state law, except that the state may file a lien for reimbursement of cost of care provided by the state during his lifetime.[26]

The trustees of the estate must have empathy and understanding and should realize that they may be facing a lifetime of administration. It may therefore be advisable to appoint alternate and successor trustees, particularly one who is the same age as or younger than the mentally retarded beneficiary.

Parents must be assisted in analyzing the costs of care for a person who is mentally retarded. In Mississippi's state institutions, the average cost of care now amounts to over $2,000 per month. Therefore, it is obvious that only exceedingly wealthy parents can provide for the total cost for many years. The estates of the vast majority of parents could only cover those things not covered by the government. These are the special extras, those things that the state does not well provide, such as spending money, television sets, recreation, and vacations.

Protection and Advocacy

The Governor's office in Mississippi, under the Federal Developmental Disabilities Act, established a system of protection and advocacy on behalf of mentally retarded persons, and this agency is separated from any agency serving retarded individuals. In Mississippi, this protective and advocacy agency has been separated from state bureaucracies in an attempt to provide truly independent, impartial aid. Many professionals feel that this arrangement is necessary because of an imcompatible conflict of interest between advocacy/protection and social service delivery. This advocacy/protection agency is administratively and financially separate from any service delivery agency and has the status of a private non-profit organization; however, this concept has yet to prove itself in Mississippi.

A basic principle needing support in the field of mental retardation is that where conflicts of interest exist, they must be reduced to the minimum. Probably no person rendering direct services to the mentally retarded should also serve as his guardian. Even families of retarded persons may have conflicts of interest when they are acting on behalf of their own family. This concern is best expressed by the official statement of the American Association on Mental Deficiency on the rights of mentally retarded persons:

> "A retarded individual frequently requires the good offices and efforts of nonrelated citizens in order to have his or her welfare safeguarded. In most instances, this fellow citizen will be a member of the retarded individual's family. Occasionally, however, it becomes necessary to have an unrelated citizen or agency act in the retarded person's behalf. The appointment of such a guardian is generally made by the courts; the guardian may be responsible both for the retarded person's estate and for his person. Such appointments should continue to be made by the courts, but only with competent professional advice. The guardian of a retarded individual should not be a public official responsible for the direct and immediate care and management of that particular person.
>
> It is the responsibility of the guardian to determine, in a manner consistent with reliable contemporary knowledge, the extent to which the individual with whose care he or she is entrused can function independently, to determine the extent of that person's ability to enjoy and exercise his or her rights, and to seek the exercise thereof."[29]

Finally, the American Association on Mental Deficiency's statement on human rights of persons who are mentally retarded should be in the minds and hearts of lawyers, parents, and other concerned citizens when planning for the future of retarded citizens:

> "Mentally retarded citizens are entitled to enjoy and to exercise the same rights as are available to nonretarded citizens, to the limits of their ability to do so. As handicapped citizens, they are also entitled to specific extensions of, and additions to, these basic rights, in order to allow their free exercise and enjoyment. When

an individual retarded citizen is unable to enjoy and exercise his or her rights, it is the obligation of the society to intervene so as to safeguard these rights, and to act humanely and conscientiously on that person's behalf.''[30]

FOOTNOTES

[1] American Association on Mental Deficiency, Manual on Terminology and Classification in Mental Retardation 5 (H. J. Grossman ed. 1977).

[2] *Id.* at 11-12.

[3] *Id.* at 18.

[4] *Id.* at 19.

[5] *Id.*

[6] *Id.*

[7] Mann and Parker, *Legal Status of the Mentally Retarded and Mentally Ill in Mississippi,* 41 MISS. L. J. 78, 86 (1969).

[8] Manual on Terminology, *supra* note 1, at 49-68.

[9] President's Task Force on the Mentally Handicapped, Action against Mental Disability (1970).

[10] Eyman, Keevan, Tarjan & Wright, *Natural History of Mental Retardation: Some Aspects of Epidemiology,* 77 Am. J. Mental Deficiency 370 (1973).

[11] N. Robinson & H. Robinson, The Mentally Retarded Child 37-42 (1976).

[12] J. Mercer, Labeling the Mentally Retarded (1973).

[13] Mississippi State Department of Education, Data Report on Programs in Exceptional Children (1981).

[14] B. Farber, Mental Retardation: It's Social Consueqence (1968).

[15] 42 U.S.C.A. § 6001 (7), (8) (Supp. 1981).

[16] Zigler, *Developmental Versus Difference Theories of Mental Retardation and the Problem of Motivation,* 73 Am. J. Mental Deficiency 536-556 '(1969).

[17] W. Wolfensberger, The Principle of Normalization in the Human Services Professions 28 (1972).

[18] Nirje, *The Normalization Principle,* in President's Committee on Mental Retardation, Changing Patterns of Residential Services for the Mentally Retarded 231-240 (R. Kugel & A. Sheaner ed. 1976).

[19] Nirje, *The Normalization Principle,* in President's Committee on Mental Retardation, Changing Patterns in Residential Services for the Mentally Retarded 51-57 (R. Kugel & W. Wolfensberger ed. 1969).

[20] Wyatt v. Stickeny, 344 F. Supp. 387 (M.D. Ala. 1972).

[21] National Association for Retarded Children, How to Provide for their Future 6 (1978).

[22] *Id.*

[23] President's Panel on Mental Retardation, Report of the Task Force on Law (1963).

[24] How to Provide for their Future, *supra* note 21, at 12-13.

[25] Report of the Task Force on Law, *supra* note 23, at 25.

[26] American Association on Mental Deficiency, Policy Statement on Guardianship.

[27] How to Provide for their Future, *supra* note 21, at 10-11.

[28] *Id.* at 13-14.

[29] Official Statement of the American Association on Mental Deficiency: *Rights of Mentally Retarded Persons,* 1973 Mental Retardation 11, 56.

[30] *Id.* at 58.

CHAPTER ONE

SUPPORT OF THE RETARDED CHILD-GOVERNMENT ASSISTANCE

A number of government programs presently pay benefits to retarded persons. Since these benefits serve as a means of support for the retarded child, continued qualification of the child for benefits can be a determinative factor in estate planning for the parents. Accordingly the following discussion reviews the major benefits available to a retarded person, focusing specifically on certain asset and income limitations to qualification for such assistance.

SUPPLEMENTAL SECURITY INCOME

Supplemental Security Income[1] is paid to persons who are sixty-five (65) years of age or older, or needy people of any age who are blind or disabled.[2] The federal government administers this program through the Social Security Administration, which makes payments to recipients, determines eligibility, and maintains recipient's records. The state's Disability Determination Services, an arm of the Social Security Administration, determines the question of a claimant's disability. States can supplement this program by providing Medicaid, food stamps, and other social and rehabilitation services to eligible persons.

SSI payments are made to any needy person who is disabled. For SSI purposes, a person is disabled if he is unable to engage in substantial gainful activity because of a physical or mental impairment which can be expected to last for twelve (12) months or longer.[3]

A person is eligible for SSI if he has little or no regular cash income and owns few assets which can be converted to cash. SSI will supplement whatever income is available to that person from other sources including Social Security benefits. In determining the eligibility of a blind or disabled child who is under eighteen (18) years of age and living at home, a portion of the parent's income and assets are treated as belonging to the child.[4] The child's portion is determined after making allowances for the working and living expenses of the parents and other children who live in the home. A retarded adult's own income and assets are considered in deciding his eligibility.

A retarded child under age eighteen (18) is considered disabled if his IQ is less than sixty (60); or if his IQ is sixty (60) to sixty-nine (69), he is dependent upon others for basic personal needs and he has a physical or other mental impairment that restricts functions and development; or if achievement of developmental milestones is no greater than that generally expected of a child half the applicant's age.[5] A retarded adult is considered disabled if his IQ is less than fifty (50); or, if his IQ is fifty (50) to sixty-nine (69), he has an inability to perform routine repetitive tasks, and he has a physical or other mental impairment resulting in restriction of function; or, he has a severe mental or social incapacity which creates a marked dependence on others for meeting personal needs.[6]

A child cannot receive both SSI payments and Aid for Dependent Children. If a child qualifies for both, the parent or guardian must choose between the two.[7]

BENEFITS

The amount of benefits payable under SSI depends on the recipient's marital status, his income, and his assets.[8] These amounts also fluctuate each year with the cost of living. However, if the SSI recipient resides in a public or private institution, such as a retardation center, which is receiving Medicaid payments covering more than fifty percent (50%) of the cost of the care, the recipient is not entitled to the full SSI payment otherwise available to him.

ASSETS AND INCOME LIMITATIONS

Ownership of assets in excess of certain levels, set by the government for single persons and married couples, will prevent qualification for SSI. Assets, as defined by the SSI program, include savings accounts, stocks, bonds, jewelry, and certain other valuables.[11] Not included as assets are the applicant's home and any adjacent land, a limited amount of equity in personal effects or household goods, and certain life insurance policies. One automobile will be excluded if used by persons in the household as transportation to a job or a place for regular treatment of a specific medical problem, if modified for use by a handicapped person, or if the fair market value of the automobile does not exceed a specified limit. If the applicant's countable assets exceed the asset limitation by a small amount, the person may still qualify for SSI payments if he agrees to sell the excess assets.[12]

Another restriction is placed on the amount of income that an applicant may receive.[13] A small amount of unearned income and earned income will not reduce the SSI payment. However, one-half of any excess earned income and all excess unearned income generally will reduce SSI benefits. Some reduction in benefits also may be required, if the applicant resides in the household of another person.[14]

Earned income includes food, shelter, clothes, and other in kind items, and funds provided to pay for these items; Veterans Administration benefits; railroad benefits, annuities, worker's compensation, unemployment insurance benefits, social security benefits; prizes, settlements, and awards.[16] Also treated as unearned income are proceeds of life insurance policies, gifts and contributions in cash and kind, support and alimony payments, inheritance in cash and property, rents and interest, and union benefits.

While most of the earned and unearned income an applicant receives is counted in determining his eligibility, some is not counted.[17] Income not counted includes refund of taxes paid on real property or on food purchases; assistance by a state or local political subdivision which is based on need; tuition and fees paid by grants, scholarships, and fellowships; homegrown produce consumed by the individual and his family; limited amounts of irregular and infrequent earned income and unearned income necessary for the fulfillment of an approved plan to achieve self-support; food stamp assistance; housing assistance from federal housing programs operated by state and local subdivisions; and benefits, compensation, or items from ACTION programs operated by State and local subdivisions.[18]

When an applicant's parent, guardian, or any responsible individual visits the Social Security office to apply for SSI benefits for a retarded individual, he should take with him the applicant's social security number, birth certificate, medical records, asset and income information, and information about living arrangements. Changes in the living conditions of the recipient should be reported to the Social Security office. If the applicant is unable to manage his own funds, a representative payee will be appointed for him.

MEDICAID

Medicaid is administered by the Department of Public Welfare.[19] The department determines a person's eligibility and certifies for Medicaid those people who are aged, blind, or disabled and who do not have sufficient income or resources to meet their living expenses.

The Medicaid program cannot reimburse the Medicaid recipient. Reimbursements are made only to the provider of the services and only if that person or institution is willing to file for payment with the Medicaid program.[20]

Several requirements must be met before an applicant is eligible for Medicaid benefits.[21] The applicant must be an adult who is sixty-five (65) years of age or older, blind, or disabled; or a child under eighteen (18) years of age who is blind or disabled (blindness and disabled standards are set by the Welfare Department). The applicant cannot be an inmate in a public institution such as Whitfield or Parchman. He must be a resident of the state and a resident of the county in which he makes his application.

ASSET AND INCOME LIMITATIONS

In order to qualify for Medicaid, the applicant must establish that he does not own a home having a county assessed valuation in excess of specified limits.[22] In addition, he must show that the combined value of his cash and other property falls below the applicable asset limitation. The amount of this limit is dependent on whether the applicant supports other persons. An applicant will be disqualified if he has transferred property within the past two years in order to avoid these asset limitations and become eligible for Medicaid.

Further, the applicant must establish that he does not have sufficient income to cover his living expenses and his medical expenses. Should the applicant have income in excess of the limits allowed,[23] he may still qualify for Medicaid. In such a situation, the applicant spends down the portion of his income in excess of the limits set by Medicaid so that he becomes eligible for Medicaid.[24] To qualify, the applicant must show that his medical expenses will consume his excess income. This provision, therefore, permits Medicaid coverage for persons who incur large medical expenses, either at one time or over a longer period of time, and lack sufficient funds to pay these expenses.

Once a person has qualified for Medicaid benefits, he may continue to receive payments indefinitely.[25] However, these payments will last only so long as he satisfies all eligibility requirements and his income does not exceed the limit set by Medicaid.

BENEFITS

Medicaid pays for medical and health related expenses,[26] including certain hospital care and skilled or intermediate care for the mentally retarded, such as care in retardation centers and nursing homes. Among other benefits provided are the costs of a limited number of physician visits and drug prescriptions, physician's services such as surgery, and some dental treatment. If ordered by the recipient's doctor, home health care, medically necessary durable equipment and supplies furnished by a home health agency, and laboratory work also may fall within Medicaid's coverage. Medicaid benefits are coordinated with Medicare, so that Medicaid will pay certain deductibles required under both the hospital and medical benefit programs of Medicare.

A person eligible for Medicaid while residing in his own home, who later needs nursing home care such as that provided by a retardation center, is automatically eligible for Medicaid payments for the cost of care in such institutions.

MEDICARE

Medicare is a federal health insurance program enacted to pay for the high cost of health care for people sixty-five (65) years of age or older, and for severely disabled people under sixty-five (65) years of age. The program is administered by the Health Care Financing Administration, through the Social Security Administration. Medicare has two programs—hospital insurance and medical insurance. The hospital insurance portion of Medicare pays for costs of inpatient hospital care and for certain follow-up care. The medical insurance portion pays for costs of doctor's services, out-patient hospital services, and other medical expenses and services not covered under hospital insurance.

Generally, anyone who is sixty-five (65) years of age or older is eligible for Medicare. Also eligible are disabled people under sixty-five (65) years of age who have been entitled to Social Security disability benefits for twenty-four (24) consecutive months or railroad retirement benefits based on disability for twenty-nine (29) consecutive months. These persons will receive hospital insurance automatically.

BENEFITS-HOSPITAL INSURANCE

Medicare hospital insurance pays for medically necessary care at a participating facility. This care includes inpatient care at a hospital, nursing or rehabilitation care at a skilled nursing facility or specially qualified facility, and home health care provided by a home health agency. Medicare hospital insurance also covers other services such as the costs of a semi-private room and meals, regular nursing services, special care units such as intensive care units, drugs, supplies, equipment, any services ordinarily furnished to inpatients of hospital or skilled nursing facilities, and certain services provided by a home health agency.

However, Medicare hospital insurance does not pay for all medical expenses incurred by the claimant. No coverage is provided for services or supplies that are not necessary for the diagnosis or treatment of an illness or injury, or for convenience items.

BENEFITS-MEDICAL INSURANCE

Anyone who is sixty-five (65) years of age or older or who is eligible for Medicare hospital insurance qualifies for Medicare medical insurance. If an individual is receiving Social Security benefits or railroad retirement benefits, he will be enrolled automatically for medical insurance at the same time he becomes entitled to Medicare hospital insurance.

Medicare medical insurance pays for services determined to be medically necessary. Coverage extends to costs of physician's services, certain outpatient hospital services, and home health care. Benefits may also cover many other services and expenses determined to be medically necessary, such as outpatient therapy and additional health services prescribed by a doctor, the cost of artificial limbs, and expenses incurred for durable equipment used in the home.

Again, medicare medical insurance does not pay all expenses or services charged to the Medicare claimant. No benefits are paid for services or supplies that are not necessary for the diagnosis or treatment of an illness or injury or for routine physical checkups and tests directly related to such examinations.

VETERANS ADMINISTRATION BENEFITS

The Veterans Administration can provide medical care for the spouse and children of a veteran honorably or generally discharged from service, if the veteran and his family cannot receive care under certain other assistance programs such as Medicare. These benefits are paid only to families of a veteran who is either totally disabled or deceased as a result of a service - connected disability.

Three types of service compensation are also provided by the V.A. to families of deceased veterans, including dependency and indemnity compensation payments to a surviving family of a veteran who died of a service-connected death after January 1, 1957; death compensation payments to a surviving family of a veteran who died of a service-connected death before January 1, 1957; and death pension payments to a surviving family of a veteran who died of a non-service connected death. These compensation payments are authorized for widows, widowers, unmarried children under eighteen (18) years of age and helpless children of certain service personnel or veterans. A helpless child is one who becomes permanently incapable of self-support because of a mental or physical defect before reaching the age of eighteen (18). He may receive compensation as long as the condition exists or until he marries.

Widows, widowers, and unmarried children (under the age of eighteen (18) years) of deceased veterans of any war or conflict since the Spanish-American War may be eligible for pension benefits based on need. Children who became permanently incapable of self-support because of a mental or physical defect before reaching eighteen (18) years of age may receive these benefits as long as the condition exists or until marriage. However a pension is not payable to those persons whose estates are sufficient to provide for their maintenance.

Applications for compensation benefits are made at a V.A. office. Applications for medical benefits are made at a V.A. medical center. The amount of compensation or pension benefits to which a family is entitled is determined by the size of the family and current applicable rates.

SOCIAL SECURITY FOR A DISABLED CHILD

Social Security provides monthly benefits for a qualified worker and/or his dependents upon the retirement, disability, or death of the worker.[27] Normally, benefits received by a child under this program will be terminated when the child reaches eighteen years of age. However, benefits may continue indefinitely if the child is disabled.[28]

A mentally retarded child who is so seriously handicapped that he is disabled may become eligible for monthly Social Security benefits when the worker becomes eligible or upon the death of the worker, if the child was disabled before reaching twenty-two (22) years of age and has continued to be disabled thereafter.[29] The fact that the child is mentally retarded does not insure that he will be considered disabled for Social Security purposes. Under Social Security, he is considered disabled only if he has a physical or mental condition which prevents him from doing substantial gainful work or which may be expected to last at least one year.[30] If a retarded child is receiving benefits as a child of a qualified worker, he or his representative should notify the Social Security office of his condition prior to his attaining the age of eighteen (18) years and apply for benefits as an adult disabled in childhood. If he is found to be disabled, his benefits will continue without interruption.

An unafflicted child whose benefits were terminated at age eighteen (18) can have those benefits reinstated if he becomes disabled before reaching age twenty-two (22). If disability begins between the ages of eighteen (18) and twenty-two (22), an application should be filed at the time a qualifying parent begins drawing retirement or disability benefits or dies. Monthly payments can be reinstated if a person previously received benefits as a disabled child, later recovered, but within seven (7) years, again became disabled.[31]

Application for benefits for a retarded person must be accompanied by evidence demonstrating that the person has a severe disability, which began before age twenty-two (22) and has continued thereafter with little likelihood for improvement. A report from the family doctor or the institution at which the person resides as a patient is usually submitted. Also, proof of the disabled person's age and his relationship to the worker is necessary.

Earned income of the recipient in excess of applicable limits[32] may reduce his Social Security benefits. Earned income includes wages of an employee, net earnings from self-employment, dismissal payments, bonuses, commissions, fees, and certain cash tips.[33]

Most unearned income of the recipient will not reduce his Social Security benefits. Unearned income includes interest on savings accounts, investment income in the form of dividends from stocks, annuities, Social Security benefits, pensions, other retirement pay, Veterans Administration benefits, gain from the sale of capital assets, gifts, inheritances, and rental income from real estate.

If the recipient of these benefits is unable to manage his funds, a representative payee will be appointed to manage his funds. The person appointed is usually the recipient's parent, legal guardian, or the institution at which he resides.

FOOTNOTES

[1] 42 U.S.C.A. § 1381 *et. seq.* (1978).

[2] 20 C.F.R. § 416. 901 *et seq.* (1981).

[3] 42 U.S.C.A. § 1382c(a) (1978).

[4] 42 U.S.C.A. 1382c(f) (1978).

[5] U.S. Department of Health, Education and Welfare, SSI for Retarded People, 5 (1979).

[6] *Id.*

[7] *Id.*

[8] 42 U.S.C.A. § 1382b (1978).

[9] 42 U.S.C.A. § 1382a (1) (B) (1978).

[10] 42 U.S.C.A. § 1382b (1978).

[11] 42 U.S.C.A. § 1382b(a) (1978).

[12] 42 U.S.C.A. § 1382b(b) (1978).

[13] 42 U.S.C.A. § 1382a (1978).

[14] 42 U.S.C.A. § 1382a(a) (2) (1978).

[15] 42 U.S.C.A. § 1382a (a) (1) (1978).

[16] 42 U.S.C.A. § 1382a (a) (2) (1978).

[17] 42 U.S.C.A. § 1382a (b) 1978.

[18] *Id.*

[19] MISS. CODE ANN. § 43-13-101 *et. seq.* (1972).

[20] 42 U.S.C.A. § 1396 *et. seq.*, (1978) (Title XIX.)

[21] 42 U.S.C.A. § 1396d (1978); MISS. CODE ANN. § 43-29-3 (1972); 42 U.S.C.A. § 1396a (a) (1978).

[22] Mississippi State Department of Public Welfare, Qualifying for Medicaid in Miss.,(1980).

[23] 42 U.S.C.A. § 1396a (f) (1978).

[24] 42 U.S.C.A. § 1396a (f) (1978); Williams v. St. Clair, 610 F 2d.1244 (1980).

[25] 42 U.S.C.A. § 1306a (a) (3) (1978).

[26] 42 U.S.C.A. § 1396d (a) (1978); 42 USCA § 1396a (a) (1978); MISS. CODE ANN. § 43-13-117 (Supp. 1979).

[27] 42 U.S.C.A. § 401 *et. seq.* (1978).

[28] 42 U.S.C.A. § 402(d) (1978).

[29] *Id.*

[30] 42 U.S.C.A. § 402(d) (1978); 42 U.S.C.A. § 416(i) (1978).

[31] 42 U.S.C.A. § 402(d) (1978).

[32] *See* 42 U.S.C.A. § 403(b) (f) (1978).

[33] 42 U.S.C.A. §§ 409, 411 (1978).

CHAPTER TWO

SUPPORT OF THE RETARDED CHILD-FAMILY ASSISTANCE

Support for a retarded child may be available from private sources such as amounts provided by a parent, assets of the child's separate estate, or a trust or other similar fund created for support purposes. The extent to which such means of private support are required by law and the extent to which such sources or assets can be reached for reimbursement by a provider of services to the child raise some complex issues hereinafter discussed.

A PARENT'S OBLIGATION OF SUPPORT

A parent is liable for the support of his minor children. This well-settled principle of common law[1] is recognized by statute in Mississippi.[2] The courts traditionally have placed the primary responsibility for such support on the father, holding the wife secondarily liable.[3] This right of support in the minor child arises out of the marriage contract.[4]

Somewhat unsettled in this state, however, is the extent, if any, of a parent's liability for the support of an adult child. The courts have held that a parent generally is not obligated to support an adult child if the adult child is capable of self-support.[5] Whether an obligation exists if the adult child is not capable of self-support is unclear.

Courts in some jurisdictions have held that a parent's obligation or duty of support continues unchanged after the child becomes an adult if the child is unable to care for himself due to infirmities of the mind or body.[6] Other courts, however, have found no such continuing duty in the absence of a statute specifically imposing that obligation.[7] Another view adopted by certain courts limits the obligation to support an adult child to situations in which the child was living at home and was incompetent at the time he reached majority.[8] A few jurisdictions have imposed such a duty even when the child was not living at home when he reached majority, requiring only that the child be incompetent at that time.[9] As a general rule, any obligation of support imposed on a parent ceases once the adult child no longer needs that support.

Although no statute in Mississippi deals directly with this issue, several statutory provisions suggest that a parent may be obligated to support an adult child in certain circumstances. One such statute is the pauper statute,[10] which requires parents and certain relatives to provide support for a needy child or relative. Although pauper statutes have been challenged as unconstitutional, they have generally been upheld as a legitimate exercise of legislative power.[11] A second statute empowers the hospital reimbursement commission to assess patients, their estates, and "all persons legally liable" for costs of care furnished the patient by a state institution.[12] This latter provision is made applicable to patients in retardation centers.[13]

Although the courts of this state have not made a definitive statement on the parent's obligation to support an adult retarded child, two cases, in disposing of other issues, have commented on the liability of such parents and the applicability of the statutes previously mentioned. In *Holsomback v. Slaughter,*[14] the court addressed the issue of whether certain property qualified as homestead property exempt from execution of a judgment lien. Mrs. Holsomback, a widow, was supporting a son in college and an adult daughter who was mentally afflicted and temporarily residing in a hospital. In reaching its decision on the status of the property, the court stated that Mrs. Holsomback was not relieved of her duty of caring for her afflicted daughter. Referring to the Mississippi pauper's statute,[15] the court further noted that a parent is obligated to maintain dependent members of her family who are unable to care for themselves. Although these statements were not central to the issue before the court, they do indicate a predisposition on the part of the court to impose such an obligation if directly faced with that issue.

In *Watkins v. Watkins,*[16] however, the court stated that it could find no statute authorizing the Chancery Court to impose a duty on parents to support an adult child. The court did not refer to or discuss Mississippi's pauper statute or the *Holsomback* case. This decision focused on a father's obligation to support his retarded son beyond age 21 under a divorce decree stating that all support obligations of the father terminated upon the child's attaining the age of twenty-one. The court held that the father's obligation under the decree ended when the child reached majority; however, the decision specifically stated that it made no determination concerning any support obligation imposed, by statute or judicial decision, on a parent of an adult retarded child. The court referred to a Mississippi statute which imposed liability for the cost of care and maintenance of a dependent patient in a state hospital on persons who are legally obligated to support that patient and found that statute inapplicable in the present case, since the child was not a patient in a state hospital.

The statute discussed in *Watkins* has been repealed. Nevertheless, the general reimbursement statute,[17] which authorizes the Hospital Reimbursement Commission to assess costs of services against patients or other persons legally liable for those costs, continues to be applicable to persons in state institutions such as retardation centers.[18] In accordance with this statute, parents of a retarded child, either a minor or an adult, may be liable for the cost of institutional care provided that child. Amounts to be collected from such persons are set by the Hospital Reimbursement Commission[19] and are based on a sliding scale, which generally takes into account that person's gross income, the number of his dependents, and the general cost of maintaining a family of that size. The reimbursement statute requires the Commission to establish policies on reimbursement which will avoid an undue hardship on the parent or the persons obligated for his support. If the fees set by the Commission are not paid, the Commission can institute proceedings against the person liable for the charges where such action is deemed necessary.[20] The statute, however, does not specify which assets of either the patient or other persons liable may be reached by the Commission in obtaining reimbursement.

A related question is the extent to which a parent is obligated to support a child or an adult incompetent child after the parent's death. The general rule in Mississippi is that the parent is not obligated to support any child after his death,[21] with one exception. Mississippi law provides for a one-year support allowance out of the assets of the parents' estate for children being supported by him at the time of his death.[22] Apart from this allowance, the parents are not obligated beyond death; however, a parent can bind himself to provide support after his death by executing a contract or providing for it in his will.[23]

CHILD'S ESTATE

Even if a child has his own estate or trust created for his support, parents who are able to support and maintain a child are not relieved of their legal obligation to do so. They are not permitted to resort to the child's separate estate or income earned by a trust created for the child, unless they are unable to support the child adequately. The parents, however, need not be destitute in order to resort to the child's estate. They will be permitted to use the child's assets for support of that child if necessary to provide for his accustomed standard of living.[24] To determine if the parents' income is sufficient for the support of their child, both the parents' and child's income will be considered, as well as the number of dependents supported by the parents' income, other expenses of maintaining the family and the physical ability of the parents to earn a living.[25]

Where a gift or bequest has been made to the parents or their child, upon condition that the property be used for the child's support, the parents may use the income and/or principal from that gift to provide reasonable support for the child, regardless of the parents' ability to support the child without the gift. The parents may use all of the income for that purpose even though the parents have been providing that support for a smaller monetary amount. If the parents are not able to support the child, they will be allowed to use as much of the gift property as is necessary to support the child.[26]

If a trust is created, requiring that the income be used for support of a child, the trustee is obligated to pay the income to the child's parents regardless of the parents' ability to support the child; however, where the trustee has discretion as to the payment of income for the support of the child, the parents cannot force the trustee to exercise his discretion in favor of the child if the parents are able to support that child. If the parents cannot furnish adequate support, the trustee may be directed to pay over an amount sufficient to provide the child with a reasonable standard of living.[27]

The child's estate is also subject to possible attachment for costs of state institutional care under the same reimbursement statutes applicable to parents.[28] In fact, these statutes require that reimbursement first be assessed against the patient or the patient's estate.

TRUST ASSETS

A parent or other relative, who creates a trust, particularly a testamentary trust, for the benefit of a retarded child may wish to prevent invasion of that trust by public authorities seeking reimbursement for the cost of care furnished the child. No Mississippi case focuses on the status of such a trust from the standpoint of the reimbursement issue; however, cases in other states shed insight into trust provisions which may serve to insulate these trusts from attack by such authorities.

A support trust is clearly subject to attachment by public authorities furnishing support to a retarded child.[29] A support trust requires the trustee to pay to the beneficiary the amount of trust income and corpus necessary for the education or support of the beneficiary.[30]

On the other hand, the trustee of a discretionary trust is required to pay the beneficiary only that amount of trust income or corpus that the trustee, in his sole discretion, deems necessary to maintain the beneficiary in accordance with a standard of support and/or health[31] specified by the trust instrument.[32] Many courts have held that a trustee of a discretionary trust can be compelled to invade the corpus if the trustee has abused his discretion.[33] Some of these courts have found the fact that the trust beneficiary is receiving public assistance sufficient evidence that the beneficiary is in need and that the trustee has abused his discretion.[34] A trust, whereby the trustee was granted discretionary powers to invade the corpus to pay the cost of any serious illness or emergency that might befall the beneficiary, has been held to imply authorization of the trustee to invade the corpus for the beneficiary's maintenance and support. The trustee's refusal to invade the corpus to pay for the beneficiary's care in a public mental institution was held to be an abuse of this discretion.[35] Further, some courts have presumed that the testator did not intend that the life beneficiary become a burden on any publicly funded program. These courts have required the trustee to invade corpus to pay for public assistance furnished the trust beneficiary.[36]

A contrary view recently has been taken by a New York court, which held that public assistance is now considered a right[37] rather than a gift.[38] The court held that the testator intended to take advantage of this right and refused to order invasion of trust corpus to pay the cost of caring for the trust beneficiary in a public psychiatric center.[39] Courts of two other jurisdictions also have refused to order similar invasions of trust corpus to pay for the beneficiary's care provided by the state. One of these cases relied on the small amount of trust corpus as an indication that the testator intended the trust to supplement benefits available through public assistance.[40] A second court argued that, since the testator had no duty to support his adult child, public policy did not prevent the testator from providing the child with extra benefits not furnished by the public institution.[41] Other courts have held that an invasion of corpus for the beneficiary's support or education can be ordered only when all persons having a beneficial interest in the trust consent to such invasion.[42]

Since many of the cases on the attachment issue were decided prior to passage of legislation offering major governmental assistance such as medicaid, few predictions can be made on the outcome of similar cases in the future. Mississippi's courts have not ruled on whether a discretionary trust can be invaded to repay public assistance provided to the trust beneficiary. Insulation from attachment by public authorities, therefore, cannot be guaranteed regardless of the use of specific trust provisions prohibiting invasion by creditors and providers of services; however, incorporation of certain provisions in a discretionary trust, in which a retarded person is beneficiary, can reduce the possibility of such attachment. These provisions include a spendthrift provision prohibiting attachment by providers of services; a statement of intent that trust distributions supplement benefits offered through government assistance; and a termination clause prohibiting further distributions to a retarded beneficiary upon ruling by a court of competent jurisdiction that the trust can be attached by creditors of the retarded beneficiary, or that the beneficiary is ineligible for governmental assistance due to the establishment of the trust.[43].

FOOTNOTES

[1] Atkins v. Curtis, 259 Ala. 311, 66 So. 2d 455, 458-60 (1953); *See generally* Annot., 1 A.L.R. 2d 910, 914 (1948); 59 AM JUR *Parent and Child* §102 (1971).

[2] MISS. CODE ANN. § 93-13-1 (1972).

[3] Simpson v. Rast, 258 So. 2d 137 (Miss. 1972); Rasch v. Rasch, 250 Miss. 885, 168 So. 2d 738, 744 (1964)); Crum v. Upchurch, 232 Miss. 74, 98 So. 2d 117 (1957); Kearney v. Kearney, 178 Miss. 766, 174 So. 59 (1937); Runnells v. State, 154 Miss. 621, 122 So. 769, 770 (1929); Watts v. Smylie, 116 Miss. 12, 76 So. 684 (1917).

[4] Rasch v. Rasch, 250 Miss. 885, 168 So. 2d 738, 744 (1964).

[5] Atkins v. Curtis, *supra* note 1 at 458-60 (1953); Wright v. Coleman, 137 Miss. 699, 102 So. 744, 776-77 (1925); Rawlings v. Rawlings, 121 Miss. 140, 83 So. 146 (1919); Sheldon v. Sheldon, 414 N.Y.S. 2d 554 (N.Y. App. Div. 1979).

[6] *E.g.*, State Dept. of Social Welfare v. Commercial National Bank, 262 P.2d 934, 936-37 (Kan. 1953); *see* Annot., A.L.R.2d 910, 921 (1948).

[7] *See* Annot. 1 A.L.R.2d 910, 920 (1948); 59 AM JUR *Parent and Child* § 103 (1971).

[8] Murrah v. Bailes, 255 Ala. 178, 50 So. 2d 735 (1950).

[9] *See* Annot., 1 A.L.R.2d 910, 926-27 (1948).

[10] MISS. CODE ANN. § 43-31-25 (1972).

[11] *See* Annot., 48 A.L.R. 733 (1927).

[12] MISS. CODE ANN. § 41-7-79 (1972).

[13] MISS. CODE ANN. § 41-7-73 (Supp. 1980); *see id.* § 41-19-13 (1972); *id.* §§ 41-19-153, 41-4-7 (Supp. 1980).

[14] 177 Miss. 533, 171 So. 542 (1937).

[15] MISS. CODE ANN. § 5706 (1930) (current version at *id.* § 43-31-25 (1972)).

[16] 337 So. 2d 723 (1976).

[17] MISS. CODE ANN. § 41-7-79 (1972).

[18] MISS. CODE ANN. § 41-7-73 (Supp. 1980).

[19] MISS. CODE ANN. § 41-7-79 (1972).

[20] *Id.*

[21] Rienhardt v. Reinhardt, 131 So. 2d 509 (Fla. 1961); Lewis v. Lewis, 239 Miss. 728, 125 So. 2d 286 (1960); Mahaffey v. First National Bank, 231 Miss. 798, 97 So. 2d 756 (1957); Fower v. Fower, 448 S.W. 2d 585 (Mo. 1970).

[22] MISS. CODE ANN. § 91-7-135 (1972); *See* Chapter 5, Wills and Administration of Estates, at p. 83.

[23] *See* note 21 *supra.*

[24] *See* Annot., 121 A.L.R. 176, 177-86 (1939).

[25] *Id.*

[26] *Id.* at 197-200.

[27] *Id.* at 200-01.

[28] MISS. CODE ANN. § 41-7-79 (1972).

[29] *See, e.g.*, First Nat'l Bank of Md. v. Dept. of Health and Mental Hygiene, 399 A.2d 891 (Md. 1979).

[30] *Id.* at 893.

[31] The standards normally used are the "ascertainable standards" set forth in Treas. Reg. § 20.2041-1(c) (2). Powers limited by an ascertainable standard are powers exercisable for the holder's "support," "support in reasonable comfort," "maintenance in health and reasonable comfort," "support in his accustomed manner of living," "education, including college and professional education," "health," and "medical, dental, hospital and nursing expenses and expenses of invalidism." *Id.*

[32] 399 A. 2d at 893. The court held that the Department of Health and Mental Hygiene could not compel the trustee to invade trust corpus to pay for the trust beneficiary's care in a mental hospital. *Id.* at 896. ***But see*** In re Estate of Browning, 352 N.Y.S.2d 269 (Sur. Ct. 1974). In ***Browning***, a trustee was given the power to "use the income and principal of said trust to the extent that she, in her unbridled discretion, may deem necessary for the support, care and general welfare" of the decedent's sister. 352 N.Y.S.2d at 770. The court ordered the trustee to invade trust corpus to repay public assistance provided the beneficiary. *Id.* at 771.

[33] *See, e.g.*, In re Schram's Will, 268 N.Y.S.2d 814, 816 (Sur. Ct. 1966); In re Estate of Gaalen, 239 N.Y.S.2d 312, 315 (Sur. Ct. 1963).

[34] In re Estate of Gaalen, 239 N.Y.S.2d 312, 315 (Sur. Ct. 1963).

[35] In re Schram's Will, 268 N.Y.S.2d 814, 816 (Sur. Ct. 1966).

[36] *See. e.g.*, In re Will of Cooper, 349 N.Y.S.2d 613, 617 (Sur. Ct. 1973); In re Crow's Will, 288 N.Y.S.2d 965, 969 (Sur. Ct. 1968).

[37] Estate of Escher, 407 N.Y.S.2d 106, 111 (Sur. Ct. 1978).

[38] *See* In re Estate of Gaalen, 239 N.Y.S. 2d 312, 314 (Sur. Ct. 1963) (holding that charity given by the state or a political subdivison of the state to help the destitute is a gift).

[39] Estate of Escher, 407 N.Y.S.2d 106, 111 (Sur. Ct. 1978). The trustees were

> authorized in the exercise of their discretion to pay out of the principal of said fund such sum or sums as may be necessary to provide for the payment of any and all expenses necessary for the maintenance and support of my said daughter . . . by reason of any illness, accident, or other emergency.

Id. at 108.

[40] Town of Randolph v. Roberts, 195 N.E.2d 72 (Mass. 1964) (refusing to order liquidation of trust to repay part of public assistance furnished trust beneficiary by welfare department).

[41] In re Wright's Will, 107 N.W.2d 146 (Wis. 1961).

[42] In the Matter of Damon, 419 N.Y.S. 2d 742, 743 (App. Div. 1979); in re Wright's Will, 107 N.W.2d 146 (Wis. 1961) (refusing to order invasion of trust corpus to pay for the beneficiary's care in an insane asylum because, among other reasons, the remainderman's interest would be prejudiced).

[43] See Appendix A.

CHAPTER THREE

GUARDIANSHIPS

A guardianship creates a legal relationship between a guardian and his ward. A guardian is a person who is appointed by the court to protect the interests of one who is under a legal disability[1] and cannot protect his own interests,[2] such as a minor or a person of unsound mind.[3] The person placed under a guardianship is a ward.[4] A similar relationship, known as a conservatorship, may be created under Mississippi statutes, permitting the appointment of a conservator to care for the interests of a person who, due to advanced age, physical incapacity or mental weakness, is incapable of managing his property.[5] These statutes make no distinction between the responsibilities of a guardian and those of a conservator so that a conservator has the same rights and duties as a guardian of a minor and is subject to all laws applicable to a guardian of a minor.[6]

A guardian or conservator, once appointed, acts for his ward, exercising certain legal rights of his ward. A guardian or a conservator may be appointed to care for the ward's person only, the ward's property only, or both the person and his property.[7] If appointed guardian of the person, the guardian should act in the best interest of his ward to insure proper care for the ward. If appointed guardian of the property of his ward, the guardian should manage that property on the ward's behalf.

PARENT'S STATUS AS GUARDIAN

The parents of a retarded minor child are the natural guardians of the child.[8] Each parent has equal powers and, if either dies, the surviving parent becomes the sole guardian. As long as either parent is living and suitable to care for the minor child, the appointment of a guardian by the court is unnecessary.[9] This natural guardianship terminates when the child reaches the age of majority,[10] which is twenty-one years in Mississippi.[11] Accordingly, a parent of a retarded child, who has attained the age of twenty-one, may wish to petition the Chancery Court for appointment as guardian for the child.

A parent of a minor child or a child under some other legal disability may appoint a testamentary guardian for that child in an attested or holographic will.[12] Such appointment is effective only when the child has no surviving parent, and is subject to the approval of the Chancery Court.[13]

PROCEDURE FOR APPOINTMENT BY THE COURT

When both parents of a minor are dead and have not appointed a testamentary guardian, or the parents are unwilling or unsuited to act as guardian, the Chancery Court of the county of the ward's residence may appoint a guardian.[14] Application for appointment may be made by anyone filing a petition[15] with the court.[16] In selecting a guardian the court gives preference to the ward's natural guardian, or next of kin.[17] If the court sustains the petition, all court costs are paid from the assets of the ward.[18] If the petition is not granted, the person who filed the petition pays all court costs.[19] When the decision to appoint a guardian is appealed and no one is qualified to act as guardian until the appeal is decided, a temporary guardian may be appointed by the court to serve until the appeal is decided.[20] If no one else qualifies as guardian for a minor having property, the clerk of the Chancery Court will be appointed to serve.[21] Since every guardianship of a minor terminates when the minor reaches the age of twenty-one,[22] appointment of a guardian for a retarded child may become necessary when that child reaches majority. Although no specific statute sets forth a particular procedure for appointment of a guardian for a retarded adult, the Mississippi Constitution grants, to the Chancery Court, jurisdiction over persons of unsound mind.[23] Accordingly, a guardian may be appointed for a retarded adult by the Chancery Court of the county in which the retarded adult resides.[24]

A specific statute outlines the procedure for appointment of a conservator for a retarded person who reaches the age of twenty-one and has not been adjudged legally disabled.[25] In order to initiate proceedings in Chancery Court to appoint a conservator, the retarded person or one or more relatives or friends must file a petition with the court asking that a conservator be appointed.[26] The person for whom a conservator is requested is examined by two physicians,[27] and a hearing is held to determine the necessity of a conservatorship.[28] After examining the alleged incompetent physically and mentally, each physician is required to file a written report of the examination with the Chancery Clerk. Oral testimony by the physicians may be presented, but is not required. If the court grants the request, the court costs are paid from the assets of the ward.[29] If the petition is not granted, the person who filed the petition pays all court costs.[30]

DUTIES OF GUARDIAN OR CONSERVATOR

After being appointed, every guardian or conservator must post bond for an amount required by the court before he has authority to act.[31] The bond acts as security for the guardian's management of the ward's estate.[32] The court will order that the ward's property be turned over to the guardian after he qualifies to care for the ward's estate.[33] The guardian then has a duty to make a reasonable effort to find all of the ward's property located within the state and to take charge of it.[34] If the guardian or conservator has also qualified to care for the ward, the ward has a legal duty to submit to the guardian's authority.[35]

The rights, duties and responsibilities[36] are the same for a guardian appointed by either a will or the court.[37] A guardian has a duty to pay out of the ward's estate, the costs of maintenance and support for the ward and his family;[38] however, only the income from the ward's estate may be used without prior court approval.[39] Prior approval should be obtained as to the amount to be expended for maintenance and education even when only the income is needed. Failure to do so risks disallowance of the expenditure by the court[40] leaving the guardian personally liable.[41] The guardian must obtain prior court approval before spending any amount in excess of the income of the ward's estate, and will be personally liable for such expenditure if prior approval is not obtained.[42] The guardian will not be personally liable if he exceeds the estate's income in an emergency situation where prior court approval is impossible.[43] If able, the parents of a minor ward[44] are required to support the ward even though he may have a separate estate.[45] The obligation of a parent to support an adult ward is somewhat unclear, although some authority exists indicating that the obligation continues at least when the adult ward is residing in certain state institutions.[46]

A guardian cannot make personal use of the funds of the ward not needed for current expenditures.[47] Instead, the guardian has a duty to invest these excess funds according to specific statutory guidelines[48] unless prohibited from doing so or directed to another form of investment by a governing instrument such as a will, trust, or deed.[49] Before making any investment, court approval must be obtained.[50]

A guardian may, with prior court approval, change the beneficiary of the ward's life insurance,[51] pay life insurance premiums out of the ward's estate,[52] and contract for life insurance for the ward's benefit if the ward is under age fifteen.[53] A guardian may also lease,[54] sell,[55] or improve[56] the ward's land with court approval, but no court approval is necessary to vote his ward's corporate stock.[57] A guardian may sue or be sued on behalf of his ward,[58] settle any claim of the estate with prior court approval,[59] and must file necessary state tax returns.[60]

No authority exists in Mississippi concerning the right of a guardian to make gifts from the ward's estate for estate planning purposes; however, courts in some states have allowed such gifts to be made by a guardian under the doctrine of substituted judgment[61] when the court is convinced that the ward, if competent, would have made the gift.[62] Criteria, often cited by the courts as necessary before such a gift can be made by a guardian from the estate of his ward, include sufficient assets for support of the ward apart from the gift property, reduction in estate taxes accruing from the gift, and close relationship of donee (recipient of the gift) to the ward.[63]

ACCOUNTING TO THE COURT

Within three months of appointment, the guardian must give the court an inventory of all property belonging to the ward and submit annual inventories thereafter.[64] Additionally, an accounting must be filed annually, and a final accounting must be filed on termination of the guardianship.[65] An annual accounting discloses all receipts and expenditures of the ward's estate for the year covered and includes a legal voucher for each expense.[66] The final accounting consists of a statement of the balances of all annual accountings plus all other receipts and expenditures of the estate.[67] After the final accounting is approved, the liability of the guardian and his surety ends.[68]

Where appointment of a guardian is made by will, the will may waive inventory, accounting, and bond subject to the court's approval.[69] In certain other situations, the court may waive all accounting except the final accounting.[70] The court may allow the guardian a credit in the annual and final accounts for proper attorney fees expended on behalf of the estate.[71] At the time of an annual account, the court may also allow the guardian a minimum of $100 for his services;[72] however, if the guardian has acted as attorney, only proper attorney fees are allowable.[73]

MISCELLANEOUS RULES

A guardian may, with prior court approval, take the ward to live in another county in Mississippi but must qualify to be guardian in the Chancery Court of the county to which the ward has moved. Thereafter, the court in which the guardian qualifies controls the guardianship.[74] Before taking his ward out of Mississippi to live, the guardian must post bond in the full amount of the ward's personal property to be taken. The court may then approve the move.[75] A nonresident guardian of a nonresident ward having property in Mississippi is entitled to be appointed guardian in Mississippi by the Chancery Court of the county in which the property is located.[76] The normal bond requirements apply to the nonresident guardian appointed in Mississippi.[77]

All guardianships of minors terminate when the minor reaches majority[78] or dies before reaching majority.[79] The guardianship also terminates upon the death, resignation, or removal of the guardian.[80] A guardian may resign at any time[81] and may be removed by the court for any reason the court deems sufficient.[82] The court may also allow the guardianship of the property of a minor or a person of unsound mind to end if the value of the property does not exceed $2000 and no prospects exist for further receipts.[83]

LIMITED GUARDIANSHIPS

Under Mississippi law all guardians are general guardians to the extent of their appointment. A guardian can be appointed as guardian of the ward and his estate, of only the ward's estate, or of only the ward.[84] This means that a guardian in Mississippi assumes total control over the ward and/or the ward's estate. Mississippi's guardianship statutes thus assume that all mentally retarded persons are totally disabled. This assumption is unrealistic as degrees of retardation may exist requiring varying amounts of supervision and care for the retarded person. To remedy this situation, several states, including Kentucky and Washington, have adopted statutes which allow appointment of limited guardians.

A limited guardianship allows the court to impose only those limitations on the disabled person as are necessary for his or her protection and assistance. For example, the Kentucky statute requires that a jury determine whether a disability exists and, if so, the nature and extent of the disability.[87] The statute adopted by the State of Washington allows the court and/or certain state agencies to investigate the nature and extent of disability.[88] After this initial determination, the disabled person is permitted to retain all rights which he or she has been found capable of exercising without assistance.[89]

The appointment of a limited guardian is initiated by the filing of a petition for adjudication of incompetency, including consideration of the nature and extent of the alleged disability. The person alleged to be retarded is evaluated by a team of qualified individuals who submit their report to the court. Usually, this team consists of a physician to examine the subject's physical condition; a social worker to examine the environment, adaptive behavior and social skills of the individual; and a person with expertise in evaluating particular types of disability that the individual is alleged to have. A state oversight commission often is established to identify and maintain a list of individuals qualified and willing to serve on the evaluation teams.

After receiving the report of the evaluation teams, the court holds a hearing attended by all interested parties. The purpose of such a hearing is discussion of whether a guardianship is warranted in light of the evaluation team's report and, if warranted, the extent of the protection and assistance that should be furnished the retarded person. The court then imposes only those limitations which it finds necessary for the retarded person's protection and assistance.

Following the appointment of a limited guardian, the court is required to hold periodic hearings to assure that the guardianship continues only as long as is necessary. Such a hearing also provides an opportunity to adjust the limitations imposed on the retarded person as his or her abilities change. The limited guardianship concept thus recognizes that total guardianship of a retarded person is not always needed. Further, it encourages retarded persons to function independently of a guardian in those aspects of his life which he is capable of handling effectively.

SPECIAL CONSIDERATIONS FOR RETARDED PERSONS

Since a guardianship in Mississippi is general rather than limited, such appointment will restrict severely the areas in which the ward may act independently of his guardian. Accordingly, appointment of a guardian or conservator for a retarded person should be requested only when necessary to insure proper care of that person or proper management of his property. A guardianship is not always needed for such a person if a parent is living and capable of providing for these needs. The naming of a trustee, under a will or a trust agreement, to manage the property of a retarded person may secure adequate care for that person.

Upon committment of a minor having neither a natural nor a legal guardian, the North Mississippi Retardation Center may request that a guardian be appointed to protect the interests of the patient and to protect the center from liability.[90] The North Mississippi Retardation Center also recommends that a legal guardian be appointed for a dependent patient[91] who is eighteen years of age or older.[92]

A retarded person is eligible for admission to the North Mississippi Retardation Center[93] and the South Mississippi Retardation Center[94] if his parents or guardian have lived in Mississippi at least one year prior to admission.[95] Further, the retarded person must be: (1) at least five years old and retarded to the extent that he is incapable of caring for himself or in need of the center's care to be able to function in society, or (2) committed by a Chancery Court, or (3) under five years old and approved by the board of trustees of the particular retardation center.[96] A retarded person may also be referred to either retardation center for diagnosis and training without formal commitment.[97]

Neither the parent's natural guardianship of their minor child nor a court appointed guardianship terminates on the retarded person's committment to a retardation center.[98]

FOOTNOTES

[1] MISS. CODE ANN. § 93-13-38 (Supp. 1979) (duties and powers of a guardian).

[2] Prudential Ins. Co. v. Gleason, 185 Miss. 243, 187 So. 229, 232 (1939).

[3] MISS. CODE ANN. § 1-3-57 (1972); *See also id.* §§ 93-13-111, -125, -131, -135 (1972).

[4] MISS. CODE ANN. § 1-3-58 (Supp. 1979).

[5] MISS. CODE ANN. § 93-13-251 (1972).

[6] MISS. CODE ANN. § 93-13-259 (1972).

[7] MISS. CODE ANN. § 93-13-251 (1972); *id.* § 93-13-15 (Supp. 1979). Courts prefer to place the ward and the ward's estate under the same guardian. Conner v. Polk, 161 Miss. 243, 133 So. 604, 605 (1931).

[8] MISS. CODE ANN. § 93-13-1 (1972).

[9] *See* MISS. CODE ANN. § 93-13-5 (Supp. 1979).

[10] *See* Watkins v. Watkins, 337 So. 2d 723, 724, (Miss. 1976); Neville v. Guardianship of Kelso, 247 So. 2d 828, 832 (Miss. 1971); MISS. CODE ANN. § 93-13-75 (Supp. 1979).

[11] MISS. CODE ANN. §§ 1-3-21, -27 (1972). MISS. CODE ANN. § 1-3-27 (1972). There are certain situations in which the age of majority has been set at age eighteen. *See, e.g.* MISS. CODE ANN. § 93-3-11 (1972).

[12] MISS. CODE ANN. § 93-13-7 (Supp. 1979). The person named as guardian in an attested will cannot be a witness to the will.

[13] A testamentary guardian must appear before and give written notice of acceptance to the Chancery Court. If he fails to qualify within 3 months of gaining the rights of guardianship or earlier if the court so directs, the guardian will be summoned to accept or renounce the guardianship. If he fails to appear or qualify, or renounces, the Court will appoint another guardian. MISS. CODE ANN. § 93-13-9 (Supp. 1979).

[14] MISS. CODE ANN. § 93-13-13 (Supp. 1979).

[15] The form of petition and proof required by the Chancery judge of the appropriate jurisdiction may vary. *See* notes 23 through 29 and accompanying text *infra*.

[16] MISS. CODE ANN. § 93-13-13 (Supp. 1979).

[17] Connor v. Polk, 161 Miss. 243, 133 So. 604, 605 (1931) (blood relatives of a minor preferred over strangers); MISS. CODE ANN. § 93-13-13 (Supp. 1979).

[18] MISS. CODE ANN. § 93-13-111 (Supp. 1979).

[19] *Id.*

[20] MISS. CODE ANN. § 93-13-19 (1972). The temporary guardian must post bond until the appeal is decided.

[21] MISS. CODE ANN. § 93-13-21 (1972) (Supp. 1979).

[22] MISS. CODE ANN. § 93-13-75 (Supp. 1979). It is within the Chancellor's discretion to terminate the guardianship of a minor who is over eighteen years of age and married.

[23] All matters concerning minors and persons of unsound mind fall within the jurisdiction of the Chancery Court. MISS. CONST. art. VI, § 159; *see* Mabrye v. Hoge, 124 Miss. on appointment of a guardian for certain persons who have been confined to a state mental hospital for more than one year and for persons in need of mental treatment (which does not include mentally retarded persons). MISS. CODE ANN. § 93-13-125 (1972); *id.* §§ 41-21-61(c), 93-13-111 (Supp. 1979).

[24] Before age twenty-one, a guardian can be appointed due to the minority of the retarded person. MISS. CODE ANN. § 93-13-13 (Supp. 1979). (See Appendix A for a sample petition).

[25] That a conservator can only be appointed for one not under a legal disability can be implied from MISS. CODE ANN. § 93-13-251 (1972), which does not refer to the person placed under a conservatorship as a ward. Instead, the statute states that "[i]f a person by reason of advanced age, physical incapacity or mental weakness is incapable of managing his own estate, the Chancery Court . . . may . . . appoint a conservator to have charge and management of the property of such person . . .".

[26] MISS. CODE ANN. § 93-13-251 (1972).

[27] MISS. CODE ANN. § 93-13-255 (1972).

[28] MISS. CODE ANN. § 93-13-255 (1972). At least five days notice of the hearing must be given to the alleged incompetent but, for good cause, the Court may direct less notice be given. Personal service of notice must be given to the alleged incompetent's spouse or one next of kin if Mississippi residents. If the spouse or next of kin is also the petitioner, personal notice is not required. The Veteran's Administration must be given notice if the alleged incompetent is entitled to any income or benefits from the Veteran's Administration. MISS. CODE ANN. § 93-13-253 (1972). The appointment of a guardian ad litem to represent the interests of the alleged incompetent at the hearing is left to the court's discretion. MISS. CODE ANN. § 93-13-255 (1972). It is also left to the Court's discretion to allow the guardian ad litem suitable compensation. MISS. CODE ANN. § 9-5-89 (1972).

[29] MISS. CODE ANN. § 93-13-257 (1972).

[30] *Id.*

[31] MISS. CODE ANN. § 93-13-17 (Supp. 1979). Bond is not needed for the part of the estate deposited, subject to the court's discretion, in a fully insured bank or savings and loan in Mississippi.

[32] Reily v. Crymes, 176 Miss. 133, 168 So. 267 (1936) (appeal by sureties from decree holding them liable for loss to ward where guardian had converted income of ward to his own use then petitioned and received permission to borrow the funds).

[33] MISS. CODE ANN. § 93-13-31 (1972).

[34] *See* Newsom v. Federal Land Bank of New Orleans, 184 Miss. 318, 185 So. 595 (1939) (suit on behalf of ward against guardian to recover damages and losses incurred by guardian's alleged negligence in running the guardianship); In re Guardianship of Horne, 178 Miss. 714, 173 So. 660 (1937) (suit by ward attacking both the validity of an insurance policy bought by the guardian for the ward with the ward's money and the guardian's management of the ward's stock).

[35] Keith v. Miles, 39 Miss. 442, 444 (1860) (suit by ward contesting guardian's claim for reimbursement for board and school outlays which the guardian promised to pay to induce the ward to return to his control).

[36] The general powers and duties of a guardian are set forth by MISS. CODE ANN. § 93-13-38 (Supp. 1979).

[37] MISS. CODE ANN. § 93-13-11 (1972).

[38] MISS. CODE ANN. § 93-13-38 (Supp. 1979). Family is defined as the ward's spouse and children, or, if none, the father and mother, or, if none, the ward's grandmother, grandfather, sisters and brothers.

[39] MISS. CODE ANN. § 93-13-35 (1972).

[40] The court, in its discretion, sets the amount to be spent. MISS. CODE ANN. §§ 93-13-35, -38 (Supp. 1979).

[41] Neville v. Guardianship of Kelso, 247 So. 2d 828, 834-35 (Miss. 1971).

[42] Deposit Guaranty Bank and Trust Co. v. Mangum, 172 Miss. 443, 160 So. 386 (1935) (bank as guardian of non compos mentis challenged the final accounting of prior guardian who, at his discretion, expended money or ward's estate). Authorized expenditures from the ward's estate are made by selling the ward's real or personal property. If best for the ward, the court may order real property sold before personal property. MISS. CODE ANN. § 93-13-35 (1972).

[43] *See, e.g.*, Williams v. Bonner, 79 Miss. 664, 31 So. 207 (1902) (emergency medical treatment).

[44] MISS. CODE ANN. § 93-13-37 (1972).

[45] Neville v. Guardianship of Kelso, 247 So.2d 828, 832 (Miss. 1971), (construing MISS. CODE ANN. § 93-13-37 (1972) (purpose is to require parents to support their minor children if they are able).

[46] See discussion in Chapter 2, Support of the Retard Child-Family Assistance, at pp. 16-20.

[47] White v. Moore, 164 Miss. 272, 144 So. 696 (1932) (suit against former guardian attacking validity of his final accounting in which guardian charged himself 4% interest on funds borrowed from the ward and not invested at 4% as ordered by the court) (construing MISS. CODE ANN. § 1885 (1930)) (current version at MISS. CODE ANN. § 93-13-57 (1972)); MISS. CODE ANN. § 91-7-253 (Supp. 1979). Additionally, the guardian cannot loan the estate's property or funds to anyone belonging to the immediate family of the guardian or ward or to any attorney representing the guardian or the estate. MISS. CODE ANN. § 91-7-253 (Supp. 1979).

[48] Acceptable forms of investments are state, county, municipal, levee board or United States bonds; building and loan or savings and loan association shares; and qualified trust notes and common trusts. MISS. CODE ANN. § 93-13-57 (1972). An earlier version of this statute has been construed as allowing only the specified forms of investment. *See, e.g.*, In re Guardianship of Horne, 178 Miss. 714, 173 So. 660, 661 (1937).

[49] MISS. CODE ANN. § 91-13-1 (1972).

[50] MISS. CODE ANN. § 93-13-57 (1972).

[51] South v. U.S., 262 F. Supp. 321 (N.D. Miss. 1966).

[52] MISS. CODE ANN. § 93-13-39 (1972). The guardian has the authority to pay only premiums on insurance policies on the ward's life that were issued during the lifetime of the ward's parents and then only if continuance of the policy is warranted.

[53] MISS. CODE ANN. § 83-7-19 (1972). *Contra* In re Guardianship of Horne, 178 Miss. 714, 173 So. 660, (1937) (denying a guardian the right to buy life insurance on the ward's life based on a strict interpretation of the predecessor of MISS. CODE ANN. § 93-13-57 (1972)).

[54] MISS. CODE ANN. § 93-13-41 (Supp. 1979). A guardian can lease the ward's real property for a maximum term of three years without court approval or for up to six years with court approval if the guardian can show that the lease is advantageous to the ward.

[55] The ward's real property can be sold if the sale is advantageous to the ward, MISS. CODE ANN. § 93-13-51 (Supp. 1979), or if converting the property into money for reinvestment would be advantageous to the ward. MISS. CODE ANN. § 93-13-45 (1972). For sales pursuant to MISS. CODE ANN. § 93-13-51 (Supp. 1979), summons must be issued pursuant to MISS. CODE ANN. § 93-13-281 (Supp. 1979), requiring that the ward's parent or parents must be joined as defendants. If neither are living, two adult kin within the third civil law degree must be joined, but if there are none, the Chancellor may appoint a guardian ad litem.

[56] MISS. CODE ANN. § 93-13-45 (1972). The guardian cannot be authorized to improve the ward's real property if there is a chance the property may later have to be sold to pay for the improvements. Payne v. Stone, 15 Miss. 367 (1846).

[57] MISS. CODE ANN. § 79-3-63 (1972).

[58] All judicial proceedings for or on behalf of a ward must be brought in the name of the general guardian. Prior court approval is necessary before any such action can be commenced. MISS. CODE ANN. § 93-13-27 (Supp. 1979). All actions against the guardian on behalf of his ward must be brought within four years after the guardian qualifies. First National Bank and Trust Company v. Landau, 183 Miss. 651, 184 So. 618 (1938) (construing predecessor statutes of MISS. CODE ANN. § 15-1-25 (1972), which concerns actions against an executor on behalf of the testator, and *id.* § 93-13-38 (Supp. 1979)).

[59] Fox v. Fairchild, 133 Miss. 617, 98 So. 61 (1923) (suit attacking validity of an authorized settlement of a wrongful death claim by a guardian acting on the ward's behalf). Either real or personal property can be accepted in satisfaction of the claim if in the ward's best interest. MISS. CODE ANN. § 93-13-59 (1972). There can, however, be no authorization of a compromise within six months of the qualification of the guardian. MISS. CODE ANN. § 91-7-229 (1972) (allowing executors and administrators to compromise claims of their estates and made applicable to guardians by reference in MISS. CODE ANN. § 93-13-59 (1972)).

[60] MISS. CODE ANN. § 27-7-31 (3) (1972). A guardian may elect to renounce a will on behalf of his ward but only during the ward's lifetime. Estate of Mullins v. Estate of Mullins, 239 Miss. 751, 125 So. 2d 93 (1960) (administrator of husband's estate seeks to renounce will of deceased wife).

[61] *See e.g.*, In re Guardianship of Christiansen, 56 Cal. Rptr. 505 (Cal. Dist. Ct. App. 1967); In re du Pont, 194 A.2d 309 (Del. Ch. 1963). ***But see*** In re Guardianship of Estate of Neal, 406 S.W. 2d 496 (Tex. Civ. App. 1966), aff'd, 407 S.W. 2d 770 (Tex 1966) (failing to recognize the doctrine of substituted judgment as the court had statutory authority to authorize gifts from the ward's estate). Massachusetts statutorily allows court authorization of gifts from a ward's estate for estate planning purposes. The gifts are allowed when the doctrine of substituted judgment is satisfied and when the gifts are to be made from funds not needed for the ward's support and maintenance. MASS. GEN. LAWS ANN. Ch.201, § 38 (West) (Supp. 1979).

[62] In re Guardianship of Christiansen, 56 Cal. Rptr. 505, 522-23 (Cal. Dist. Ct. App. 1967) (appeal from denial of petition of guardian seeking authority to make gifts of part of property of non compos mentis to reduce estate taxes); In re Guardianship of Bohac, 380 So. 2d 550, 553 (Fla. Dist. Ct. App. 1980) (appeal from denial of guardian's petition for authority to make gifts from ward's estate to beneficiaries of the ward's will); In re Turner, 305 N.Y.S. 2d 387, 389 (N.Y. Sup. Ct. 1969) (denial of petition to reduce estate tax liability by making gifts of part of corpus of incompetent's estate to his wife and children where incompetent had shown an intention to make gifts to children only on their reaching age twenty-five).

[63] A more detailed list of the necessary criteria cited in the cases includes the following:

1) incompetent's mental and physical condition are such that restoration to competency is remote;
2) assets remaining after gifts would be sufficient to maintain the incompetent considering the incompetent's life expectancy and other contingencies;
3) donees constitute the natural objects of the incompetent's bounty by any standard;
4) transfer will benefit the incompetent by reducing estate taxes;
5) there is no substantial evidence that the incompetent as a reasonably prudent person would, if competent, not make the gifts proposed in order to reduce estate tax liability.

In re Trott, 288 A. 2d 303, 307 (N.J. Super. Ct. App. Div. 1972). *See also,* In re Guardianship of Christiansen, 56 Cal. Rptr. 505, 523-24 (Cal. Dist. Ct. App. 1967); In re Turner, 305 N.Y.S. 2d 387, 390 (N.Y. Sup. Ct. 1969).

[64] MISS. CODE ANN. § 93-13-33 (1972). The guardian can be removed or sued on his bond for failing to submit annual inventories unless he can show cause for the failure.

[65] MISS. CODE ANN. § 93-13-77 (1972); *id.* § 93-13-67 (Supp. 1979). The annual accounting shows receipt of all money, the product of the estate, sales or other dispositions of property and each item of expense for the ward's maintenance and education and for management of the estate.

[66] Vouchers are required and an account not supported by a voucher is insufficient. White v. Moore, 164 Miss. 272, 144 So. 696, (1932); MISS. CODE ANN. § 93-13-67 (Supp. 1979). A voucher must conform to the requirements of executors' and administrators' vouchers. MISS. CODE ANN. § 93-13-71 (1972). A voucher may be an ordinary bank check. Each voucher must give the name and number of the case and must be filed with the clerk. MISS. CODE ANN. § 91-7-279 (1972).

[67] MISS. CODE ANN. § 93-13-77 (1972). After the guardian makes the final settlement, the ward is summoned to show why the final account should not be approved. After examining the account, the court can issue a final decree of approval or allow only the part of the final settlement that is correct. In the decree, the court can allow the guardian up to 10% of the estate's value for his services. After the property is delivered to the ward, the guardian is discharged.

[68] Connor v. Polk, 161 Miss. 24, 133 So. 604 (1931).

[69] MISS. CODE ANN. § 93-13-7 (Supp. 1979).

[70] If the ward's funds and personal property do not exceed $3000 with no prospect of further receipt other than interest, or if the funds on hand or to be received by the guardian are paid by the welfare department or if the ward's assets consist solely of fully insured deposits with a bank or savings and loan association, the court may dispense with all but the final accounting. MISS. CODE ANN. § 93-13-67 (Supp. 1979).

[71] MISS. CODE ANN. § 91-7-281 (1972).

[72] MISS. CODE ANN. § 93-3-67 (Supp. 1980).

[73] MISS. CODE ANN. § 91-7-281 (1972).

[74] The court may also allow the guardian to take the ward's personal property to another county. MISS. CODE ANN. § 93-13-61 (1972).

[75] MISS. CODE ANN. § 93-13-63 (1972).

[76] MISS. CODE ANN. § 93-13-181 (Supp. 1980). The nonresident guardian is entitled to be substituted for a guardian appointed in Mississippi. Moore v. Jones, 99 So. 437, 437 (1924). The court, in its discretion, may allow a nonresident guardian to remove a nonresident ward's personal property from the state. Final settlement of the estate must be made and bond posted in the full value of the property to be removed. MISS. CODE ANN. § 93-13-185 (1972).

[77] MISS. CODE ANN. § 93-13-181 (1980).

[78] The guardianship may be terminated, in the court's discretion, when the ward is over eighteen years of age and married. MISS. CODE ANN. § 93-13-75 (1980).

[79] If the ward dies, the guardian's only duty or responsibility is the filing of a final account. South v. United States 262 F. Supp. 321 (N.D. Miss. 1966).

[80] When a guardian dies, resigns or is removed, another guardian may be appointed by the court. MISS. CODE ANN. § 93-13-25 (1972).

[81] *Id.*

[82] MISS. CODE ANN. § 93-13-23 (1972). What constitutes sufficient cause for removal is left to the discretion of the court. Connor v. Polk, 161 Miss. 24, 29, 133 So. 604, 605 (1931).

[83] The guardianship can be terminated in this manner only if the court has the power to have the property delivered to the ward or to some other person or bank under specified conditions imposed by the court. The person receiving the property becomes liable to the court for the proper use of the money but no security is required. MISS. CODE ANN. § 93-13-75 (1980).

[84] MISS. CODE ANN. § 93-13-15 (Supp. 1979).

[85] The American Association on Mental Deficiency has established four categories of retardation based on I.Q. These catagories are: mild retardation (55-70 I.Q.); moderate retardation (40-54 I.Q.); severe retardation (25-39 I.Q.); and profound retardation (I.Q. below 25). For a further discussion of these classifications, *see* Dussault, *Guardianship and Limited Guardianship in Washington State: Application for Mentally Retarded Citizens,* 13 Gonz. L. Rev. 585, 592-95 (1978).

[86] *See, e.g.*, Ky. Rev. Stat. Ann. § 387.287 (Baldwin Supp. 1978) (authorizing appointment of limited committeeship for *adults* not totally disabled); Wash. Rev. Code Ann. § 11.88.010 (2) (Supp. 1980-81) (allowing appointment of limited guardian for *any person* not fully incompetent).

[87] Ky. Rev. Stat. Ann. § 203.022. (Baldwin Supp. 1980).

[88] Wash. Rev. Code Ann. § 11.88.010 (2). (Supp. 1980-81).

[89] Ky. Rev. Stat. Ann. § 387.287 (3) (Baldwin Supp. 1978); Wash. Rev. Code Ann. § 11.88.010 (2). (Supp. 1980-81).

[90] This is the present unofficial policy of the North Mississippi Retardation Center. Although "requests" is used, the center strongly urges that a legal guardian be appointed.

[91] North Miss. Retardation Center, Policies Governing Adult Clients, Attachment 58, sets forth 15 criteria used to determine if a patient is dependent.

[92] The center considers a patient an adult at age eighteen. This policy has been adopted in order to protect the center from liability should the patient be considered an adult at age eighteen.

[93] MISS. CODE ANN. § 41-19-9 (1972).

[94] Criteria for admission to the South Mississippi Retardation Center are the same as those for the North Mississippi Retardation Center as defined by MISS. CODE ANN. § 41-19-9 (1972); *id.* § 41-19-149 (Supp. 1979).

[95] MISS. CODE ANN. § 41-19-9 (a) (1972). The parents or guardian must file an application for admission to the North Mississippi Retardation Center. Within ten days of admission, the person alleged to be retarded is examined by a qualified physician and/or psychologist and can remain in the retardation center only if found to be retarded. All provisions of MISS. CODE ANN. § 41-19-11 (1972) also apply to the South Mississippi Retardation Center. *See id.* § 41-19-151 (Supp. 1979).

[96] MISS. CODE ANN. § 41-19-9 (1972). Any relative or citizen of Mississippi may file an affadavit with the Chancery Court alleging that a person is mentally retarded to the extent that he needs care and supervision or that he is likely to become dangerous. MISS. CODE ANN. *Id.* § 41-19-11 (b) (1972).

[97] The referral must be made by a state agency. MISS. CODE ANN. § 41-19-11 (c) (1972).

[98] North Miss. Retardation Center, Policies Governing Adult Clients, Attachment 58.

CHAPTER FOUR

ESTATE AND GIFT TAXATION

Effective estate planning involves a consideration of the laws of wills, taxes, insurance, property, and trusts, in light of personal objectives for the disposition of an estate. The estate planner will combine his knowledge of these areas of law to minimize income, estate, and gift taxes and probate costs so as to conserve the assets of the estate for transfer to the designated beneficiaries; therefore, the development of a workable estate plan, consistent with these objectives, requires review of estate assets and liabilities, formulation of estate planning goals, determination of personal and family needs, and most importantly, analysis of the impact of estate taxes.

CALCULATING ESTATE TAXES

What is the federal estate tax and how is it calculated? The estate tax is a tax on the privilege of transferring property at death levied against the estate. The estate, for tax purposes, is not synonymous with the probate estate. Accordingly, the estate tax may be assessed not only on property owned by the decedent at the time of death and passing by will or intestacy, but also on property passing by other means, such as joint ownership and contractual agreements like life insurance.

Assets includable in a decedent's estate, for estate tax purposes, are valued at "fair market value" on the date of decedent's death, or if the executor elects, on the alternate valuation date, six months after the decedent's death. Fair market value is defined as the price at which the property would change hands between a willing buyer and a willing seller, neither being under any compulsion to buy or sell and both having reasonable knowledge of relevant facts.[1]

The value of all the decedent's assets includable in his estate equals the gross estate.[2] This total is reduced by the allowable deductions[3] to yield the adjusted gross estate. From this latter amount is subtracted the marital deduction and charitable bequests[4] to reach the taxable estate[5] on which estate tax is imposed. The rate of tax currently ranges from eighteen percent (18%) on the first ten thousand dollars ($10,000) to seventy percent (70%) on an estate in excess of five million dollars. This maximum rate, however, will be lowered by five percent each year beginning in 1982 and continuing until 1985, in accordance with the following schedule:

YEAR	MAXIMUM RATE
1982	65% on amounts in excess of $4 million
1983	60% on amounts in excess of $3.5 million
1984	55% on amounts in excess of $3 million
1985	50% on amounts in excess of $2.5 million

GROSS ESTATE

The gross estate includes all the property in which the decedent has an interest at the time of death,[6] whether real or personal property, tangible or intangible, wherever it is located. In addition, other kinds of property are includable in the decedent's gross estate for estate tax purposes, some of which may not be owned by the decedent at his death. For estate tax purposes, the estate includes the following additional categories of properties:

(1) The value of gifts made within three years of the decedent's death but only if such properties are includable under categories (2), (5), and (6) below or would have been includable under such categories if the property had been retained by the decedent until his death.[7]

(2) The value of property transferred by the decedent in which certain legal or beneficial interests were retained.[8] Transfers which fall in this category are those in which the decedent retained a life interest,[9] power over income from the property,[10] a reversionary interest,[11] power to revoke, alter or terminate the transfer,[12] or power to change the beneficiaries.[13]

(3) The value of certain annuities received by a surviving beneficiary.[14]

(4) The value of jointly held property, such as checking accounts, savings accounts, and real estate; however, certain exceptions provide for inclusion of only a portion of the value of joint property such as joint property held by husband and wife and other joint interests in which the surviving co-tenant establishes a separate contribution to the purchase of the property.[15] Beginning in 1982, one-half of the value of property held jointly between spouses will be includable in the estate of the first spouse to die.

(5) The value of the property over which the decedent owned a general power of appointment.[16]

(6) The value of life insurance proceeds received by the estate on the life of the decedent or received by any beneficiary on the life of the decedent to which the decedent at the time of death retained any incident of ownership.[17]

TAXABLE ESTATE

Certain deductions are allowed against the gross estate in order to determine the decedent's taxable estate. These deductions include the following:

(1) The value of expenses and debts owed by the estate.[18] This category includes funeral expenses and other similar charges such as plot and tombstone costs; administrative expenses such as attorney fees, executor commissions, accounting and appraisal fees, and other miscellaneous expenses; and court costs. Personal obligations of the decedent that are enforceable against his estate, such as accrued interest expenses and unpaid debts, mortgages, and taxes are also deducted; however, income taxes due on income earned after the decedent's death are not deductible.

(2) The value of losses incurred while the decedent's estate is being administered and not covered by insurance.[19]

(3) The value of transfers made for certain public, charitable, and religious uses.[20]

(4) The value of property that passes to the decedent's surviving spouse.[21] Beginning in 1982, this deduction is unlimited in amount. (Mississippi does not recognize this deduction in computing Mississippi estate taxes).

By subtracting these deductions[22] from the gross estate, the taxable estate is determined. The taxable estate is increased by the decedent's adjusted taxable gifts (gifts made after December 31, 1976) to reach the sum on which the gross estate tax is computed.[23] This gross estate tax payable is reduced by any gift tax paid on gifts made after December 31, 1976, and may be further offset by the following tax credits available to estates:

(1) The unified tax credit.[24] For 1981 the unified tax credit is $47,000. This credit permits up to $175,625 in property to pass free of federal estate or gift taxes. It can be applied against either gift or estate tax liability. The unified credit, and the equivalent amount of property which can escape federal estate and gift taxes, will be increasing over the next six years in accordance with the following schedule:

YEAR	UNIFIED TAX CREDIT	EQUIVALENT EXEMPTION
1982	$62,800	$225,000
1983	$79,300	$275,000
1984	$96,300	$325,000
1985	$121,800	$400,000
1986	$155,800	$500,000
1987	$192,800	$600,000

(2) State death tax credit.[25] This credit equals state death taxes actually paid, but not in excess of certain limits imposed by statute.

(3)Gift tax credit.[26] This credit equals the amount of taxes paid on certain property which the decedent transferred during his life if that property was included in his gross estate.

(4) Federal estate tax credit.[27] This credit is available for a portion of federal estate taxes previously paid by another estate on property currently included in the decedent's estate. The property transferred must have been received by the current estate from a decedent who died within 10 years prior or 2 years after the date of death of the current decedent.

(5) Foreign death taxes.[28]

The following computation illustrates how estate taxes are computed on a gross estate of $800,000, with deductible expenses of $100,000, in which the decedent devised one-half of his adjusted gross estate to his surviving spouse and $50,000 to charity. Assume no gifts were made during the decedents lifetime and the decedent died in 1981.

Estate Tax Computation:

Gross Estate			$800,000
Less:	Funeral Expenses	$10,000	
	Administrative Expenses	30,000	
	Losses	2,000	
	Mortgages and other Debts	58,000	100,000
Adjusted Gross Estate			$700,000
Less:	Marital Deduction	350,000	
	Charitable Contributions	50,000	400,000
Taxable Estate			$300,000
Adjusted Taxable Gifts			-0-
Sum on which Federal estate tax is computed			$300,000
Gross Estate Tax			87,800
Less:	Unified Credit	47,000	
	State Debt Taxes (assume $3,600 actually paid)	3,600	50,600
Federal Estate Tax Payable			$ 37,200

The unified tax rates are applicable to both estate and gift tax caculations.[29] This unified tax system is a progressive one, much like the present federal income tax system.

ESTATE TAX RETURN FILING REQUIREMENTS

Within nine months after the decedent's death, the decedent's estate tax return (Internal Revenue Service Form 706) must be filed.[30] But an estate tax return is not always required. For a decedent dying in 1981 an estate tax return is due only if the decedent's gross estate exceeds $175,000.[31] For decedents dying in later years, the gross estate must exceed the exemption equivalent of the unified tax credit, as set forth on page 51. Thus, estates of decedents dying in 1987 and thereafter, which equal $600,000 or less, will not be required to file a return.

CALCULATING GIFT TAXES

For gift tax purposes, a gift has been made when property is transferred outright, in trust, or otherwise for less than adequate consideration.[32] The gift can be a direct or indirect transfer of real or personal, tangible or intangible property. The objective facts of the transfer and the circumstances under which it is made will determine whether a gift has been made, rather than the subjective motives or intent of the donor.[33]

Every donor may give property having a value of as much as $10,000 annually per donee free of federal gift tax;[34] however, this exclusion is available only for a gift of a present interest in property. That is, the property must be enjoyable immediately.[35] Accordingly, a father, who has three children, may transfer $10,000 to each child annually, without liability for gift taxes due to the annual $10,000 per donee exclusion. If annual gifts do not exceed these exclusions, no gift tax return is required.

For gifts made between spouses, the donor spouse obtains the benefits of the gift tax marital deduction.[36] The amount of any such gift qualifies fully for the marital deduction and no gift tax return is required. The only requirement for receiving this gift tax marital deduction is that the donor and the donee must be married at the time of the gift.[37]

Another gift tax rule, pertaining solely to spouses, permits a spouse, to "split" any gift made to a donee with the donor spouse so that the gift is treated as being given one-half by each.[38] To qualify, the gift must be made to someone other than the donor's spouse. For example, husband transfers real estate worth $40,000.00 to his daughter and son-in-law. His wife consents to split the gift so that each spouse is treated as having made a gift of $20,000 to the daughter and son-in-law ($10,000 to the daughter and $10,000 to the son-in-law). Since husband and wife each get an exclusion of $10,000 per donee, each is entitled to $20,000 in exclusions (two donees at $10,000 each). Thus, no gift tax is due on the transfer.

To determine the gift tax payable on a current taxable transfer, the value of all prior lifetime taxable gifts is added to the current taxable gift. A tentative gift tax is computed on this sum. From this tentative tax is deducted the unused unified tax credit[39] and gift taxes on prior gifts.

For example, assume a donor makes his first gift of $160,000 to his son in 1982. The tax computation is made as follows:

Gift Tax Computation:	
Gross Amount of Gift	$160,000
Less: $10,000 per donee exclusion	10,000
Gift Subject to Gift Tax	$150,000
Gross Gift Tax Payable	38,800
Less: Unified Tax Credit (Credit of $62,800 available in 1982)	38,800
Gift Taxes Payable	-0-

GIFT TAX RETURN FILING REQUIREMENTS

Gift tax returns (Internal Revenue Service Form 709) are filed on an annual basis.[40] Generally, all required returns are due on the 15th day of April after the calendar year in which the gift was made.[41]

INCOME TAXATION OF GIFTS

The donee does not include the value of property received by gift or inheritance in gross income for income tax purposes.[42] This exclusion from gross income does not extend to income generated by the gift or inherited property, and such income will be subject to income taxation upon receipt.[43]

BASIS IN INHERITED OR GIFT PROPERTY

When property is transferred from the decedent's estate, the heir takes as his basis in that property its fair market value on the date of the decedent's death or the fair market value on the alternate valuation date, if elected by the executor.[44] Accordingly, if the fair market value of the property on the decedent's death exceeds his basis in the property, that potential gain escapes federal income taxation. This basis acquired by the heir is often referred to as a "stepped-up basis."

To illustrate the stepped-up basis rule, assume a decedent purchased 100 shares of stock on June 1, 1950, at $10 per share, for a total cost of $1,000. On December 1, 1981, the decedent died, when the value of the stock had appreciated to $50 per share. The decedent's estate tax return includes the stock at the fair market value of $5,000, which would become the heir's basis in the stock. If the heir sells the stock five years later for $100 per share, only the appreciation accruing after the date of the decedent's death will be subject to taxation for income tax purposes.

Sales price 12/1/86	$10,000
Basis (fair market value 12/1/81)	5,000
Gains subject to income tax	$ 5,000

Where property is transferred by gift, however, the donee does not receive a stepped-up-basis. Generally, the donee's basis in property received by gift is the same as the donor's basis;[45] however, the donee's basis in property received as a gift may be increased by the amount of gift tax attributable to any appreciation in the gift property.[46]

MISSISSIPPI ESTATE TAX

The State of Mississippi has an estate tax[47] but no gift tax. A Mississippi estate tax return must be filed within nine months of the date of death of each resident[48] whose gross estate on the date of death has a value exceeding the allowable exemption.[49] A Mississippi estate tax return must be filed within nine months of the date of death on any nonresident[50] who owns property in Mississippi and whose total estate, wherever located, exceeds the allowable exemption.[51] In addition to the regular estate tax return, a special written notice must be filed within 60 days of the decedent's death or qualification of the executor. This notice must indicate the decedent's name and date of death, the attorney's name, the gross estate's probable value and any transfers made within two years of the decedent's death.[52]

Any estate tax due must be paid within nine months of the decedent's death unless an extension[53] is granted.[54] Interest of ½ of 1% per month must be charged on estate taxes not paid within the nine month period even though an extension may have been granted.[55] The representative of the estate is personally liable for payment of the estate tax if he or she pays any of the estate's debts before paying the estate tax.[56]

The decedent's gross estate may be valued on the date of the decedent's death or on the alternate valuation date. The alternate date is the date exactly six months after the decedent's death.[57] All values which the federal government accepts are considered prima facia correct if used on a Mississippi estate tax return.[58] A resident decedent's gross estate includes all real and personal property, whether tangible or intangible, that is located in Mississippi. Real property and tangible personal property located outside of Mississippi are not included in a resident's gross estate. Mississippi's estate tax is imposed on the value of all real and tangible personal property located in Mississippi includable in a nonresident owner's estate.[59]

Mississippi's estate tax permits the exclusion from a decedent's gross estate of the first $20,000 in life insurance proceeds payable to a named beneficiary other than the decedent's estate.[60] Additionally, each spouse is presumed to have contributed one-half of the cost of all property owned jointly by the spouses. One-half of the cost of such property is therefore included in the estate of the first spouse to die unless the surviving spouse can prove that he or she contributed more than one-half of the purchase price.[61] Furthermore, a gift within three years of death is considered prima facia evidence that the gift was made in contemplation of death. The representative of the estate bears the burden of proving that the gift was not made in contemplation of death.[62]

Several deductions from a decedent's gross estate are allowed in order to determine the net estate; however, Mississippi law does not allow a marital deduction.[63] Allowable deductions from a resident decedent's gross estate include funeral and administrative expenses, claims against the estate including unpaid mortgages and uninsured casualty losses incurred during the settlement of the estate. Also deductible are charitable donations and the amount reasonably required and actually spent for support of the decedent's legal dependents during the settlement period. While taxes which the decedent owed on the date of death are deductible, neither state nor federal estate taxes may be deducted.[64] The estate tax exemption of $175,625 is also deductible from the gross estate of a resident decedent.[65]

A nonresident decedent's estate is allowed the same exemption, exclusion and deductions as are allowed the estate of a resident decedent with the exception of charitable contributions. The amount of each deduction and exclusion is limited, however, to the fraction of the decedent's gross estate that consists of property located in Mississippi. Charitable contributions may be deducted only if the contributions are to be used in Mississippi or are contributed to a charitable institution which operates at least partly in Mississippi.[66]

The taxable estate is determined by subtracting the allowable exclusion and deductions from the decedent's gross estate.[67] The estate tax due is determined by multiplying the taxable estate by the applicable rate set forth in *Mississippi Code Annotated* § 27-9-5 (Supp. 1980).[68]

MINIMIZING TRANSFER TAXES

Two general techniques can be employed to reduce or eliminate potential estate taxes. First, lifetime gifts can be made which will reduce the value of the estate of the donor. Secondly, the remaining estate should be planned for effective use of statutory provisions exempting certain property from estate taxation. This second step centers on such areas as the marital deduction for property conveyed to the surviving spouse, the tax treatment of life insurance proceeds, and the charitable deduction for contributions to qualifying organizations.

By making lifetime gifts, the donor removes not only the gift property but also future appreciation on those assets from his estate. Further, certain assets have a much higher valuation for estate tax purposes than for gift tax purposes. For example, an insurance policy insuring the donor's life would be valued at its replacement cost for gift tax purposes. On the other hand, the face value of the policy or its proceeds would be subject to estate tax if includable in the gross estate of the insured.

When formulating a plan for making lifetime gifts, certain preliminary questions must be answered. Does the donor want to give up control of his property? The donor must release all of his interest in or control over the gift property in order to remove that property from his gross estate. Assuming that the donor is willing to make a completed gift of the property, can he afford to give up the income from the assets? Gifts may be more appropriate for donors having substantial estates. Is the donor in good health? Are the donees minors or incompetent to manage property? Is a trust needed to manage the property? Is the donee's estate so large that a gift to him or her would subject the property to a higher estate tax than if the donor retained the property himself?

A well designed gift plan will not only reduce estate taxes but can also reduce income taxes. This savings is accomplished by the transfer of income producing property from the donor to a donee in a lower income tax bracket. In selecting the property to transfer, the donor should choose property that offers potential for appreciation. Property that has already appreciated or has begun to decrease in value is not particularly well-suited for gifts.

In addition to adoption of a gift program, the donor can further reduce his estate by taking advantage of the estate tax marital deduction. Beginning in 1982, this deduction is unlimited in amount. The decedent's adjusted gross estate is reduced by the fair-market value of any property passing to the surviving spouse in a qualifying manner.[69] Such property is potentially subject to an estate tax in the estate of the surviving spouse unless she consumes it or gives it away.

In qualifying a person's estate for the marital deduction, two questions must be answered. What is the value of the adjusted gross estate before deducting the marital bequest? If the estate is less than the estate of the spouse to whom the property will be passing, it may be advisable to forego a marital deduction since inclusion in such spouse's estate will subject the property to a higher rate of estate tax. What type property interest is preferred as the mechanism for transferring property to the spouse? To qualify for the marital deduction, property must be left to the surviving spouse outright or in certain specially-drafted trusts known as a marital deduction trust or an estate trust. If such a trust is employed, the surviving spouse must receive the income for life and a general power of appointment over the corpus, allowing the surviving spouse to name her estate or someone else as beneficiary of the trust property at the time of her death. Beginning in 1982, certain life interests in property granted to a surviving spouse will also qualify for the marital deduction, if the executor so elects.

Another technique of estate planning is the removal of life insurance from the insured's estate. Proceeds from life insurance insuring a decedent's life are subject to estate tax if they are payable to his estate or if the decedent retains some incident of ownership in the policy.[70] An incident of ownership includes the right to name or change beneficiaries, borrow against the policy, or assign it. If the decedent is not the owner and has retained no interest in the policy, the proceeds pass free from estate tax in his estate, even if the decedent paid the premiums on the policy. The transfer of the policy, of course, will be subject to gift tax. Also, if the insured continues to pay the premiums after he transfers ownership of the policy, further gift taxes may be generated on the value of the premiums paid.[71]

Additional reductions in estate taxation can be achieved through bequests to qualified charities.[72] These contributions reduce the estate by an amount equal to the fair market value of the asset or assets conveyed. If property is owned which has a high fair market value but is difficult to sell due to a limited market, that asset would be an appropriate subject for bequest to a charity.

A severe problem for many estates is the lack of liquid assets available for payment of estate taxes and administration costs. This situation can exist in both large and small estates and is especially prevalent in estates which consist to a large degree of non-liquid assets, such as real estate, closely-held stocks, a farm, or a business. The problem is particularly acute if no market exists for these assets. Consequently, assets will have to be sold, often at a price below fair market value, to generate sufficient cash to pay the estate taxes, debts and administration costs of the estate.

Several techniques may be employed as a means of creating liquidity for an estate:

(1) Entering buy-sell agreements with key employees, business associates, or a closely-held corporation. By entering such agreements, the parties can set a value on the property covered by the agreement. At the date of decedent's death, that agreement generally binds his estate to sell at the specified amount. The asset will be includable in the estate at the value set in the agreement if certain conditions are met. Such an arrangement prevents a forced sale or liquidation, since the decedent's interest in the business is sold by the estate to the other party or parties soon after the decedent's death, thereby generating cash for the estate. These agreements are generally appropriate for closely-held corporations, family businesses, or partnerships.

(2) Purchasing an amount of life insurance sufficient to pay the estate taxes and other expenses. This method is particularly beneficial if a trust is named as owner and beneficiary of the life insurance proceeds, and the same trust is permitted to use the insurance proceeds to purchase non-liquid assets of the

estate. This method provides cash to the estate and allows the trust to hold the non-liquid assets until they can be sold for a fair price. Life insurance may also be used to fund the buy-sell agreements mentioned above.

(3) Paying the estate tax over a period of years. Under certain circumstances, the estate may pay a portion of its federal estate tax liability on an installment basis. This system of payment allows the property included in the estate sufficient time to generate income to pay the estate tax. Installment payment is available to estates which consist, to a large degree, of closely-held business interests.

FOOTNOTES

[1] Treas. Reg. § 20.2031-1 (6).

[2] I.R.C. § 2031-2044.

[3] I.R.C. § 2052, 2054.

[4] I.R.C. § 2055, 2056.

[5] I.R.C. § 2052.

[6] I.R.C. § 2033.

[7] I.R.C. § 2035. Excepted from coverage are gifts for which no gift tax return is required (other than exempt martial gifts).

[8] I.R.C. § 2036-2038.

[9] I.R.C. § 2036.

[10] Id.

[11] I.R.C. § 2037.

[12] I.R.C. § 2038.

[13] Id.

[14] I.R.C. § 2039.

[15] I.R.C. § 2040.

[16] I.R.C. § 2041.

[17] I.R.C. § 2042.

[18] I.R.C. § 2053.

[19] I.R.C. § 2054.

[20] I.R.C. § 2055.

[21] I.R.C. § 2056.

[22] An additional exclusion, called the orphan's exclusion, is available for limited transfers to minor children. I.R.C. §2057. However, the exclusion is not be available to estates of decedents dying after 1981.

[23] I.R.C. §2001.

[24] I.R.C. §2010.

[24] I.R.C. §2011.

[26] I.R.C. §2012.

[27] I.R.C. §2013.

[28] I.R.C. §2014.

[29] I.R.C. §2001.

[30] I.R.C. §6075.

[31] I.R.C. §6018.

[32] Treas. Reg. §25.2511-1.

[33] *Id.*

[34] I.R.C. §2503.

[35] I.R.C. §2503, Treas. Reg. 25.2503.

[36] I.R.C. §2523.

[37] Treas. Reg. §25.2523.

[38] I.R.C. §2513.

[39] I.R.C. §2505.

[40] I.R.C. §6075.

[41] *Id.*

[42] I.R.C. §102.

[43] *Id.*

[44] I.R.C. §1014.

[45] I.R.C. §1015.

[46] *Id.*

[47] MISS. CODE ANN. §27-9-1 *et. seq.* (1972).

[48] "Resident" is defined as "any person domiciled in the State of Mississippi and any other person who maintains a permanent place of abode within the state and spends in the aggregate, more than six months of the taxable year within the state." MISS. CODE ANN. § 27-9-3 (f) (1972).

[49] MISS. CODE ANN. § 27-9-23 (Supp. 1980). The applicable exemption for a decedent dying in 1981 is $161,563.00 and $175,625.00 for a decedent dying in or after 1982. *Id.* § 27-9-11 (Supp. 1980).

[50] A "nonresident" is defined as "any natural person whose domicile is without the State of Mississippi or who maintains a place of abode without the state, and spends in the aggregate, more than six months of the taxable year without the state." MISS. CODE ANN. § 27-9-3 (g) (1972).

[51] MISS. CODE ANN. § 27-9-23 (Supp. 1980). For the applicable exemptions, *see* note 49 *supra.*

[52] MISS. CODE ANN. § 27-9-21 (Supp. (1980).

[53] Extensions, not to exceed six months per extension, may be granted if payment of the estate tax would impose an undue hardship on the decedent's estate. MISS. CODE ANN. § 27-9-27 (Supp. 1980).

[54] *Id.*

[55] *Id.*

[56] MISS. CODE ANN. § 27-9-37 (1972).

[57] MISS. CODE ANN. § 27-9-7 (Supp. 1980).

[58] MISS. CODE ANN. § 27-9-29 (1972).

[59] MISS. CODE ANN. § 27-9-7 (Supp. 1980).

[60] *Id.* No such exclusion is allowed from the decedent's gross estate for federal estate tax purposes.

[61] *Id.*

[62] *Id.*

[63] Federal estate tax law allows a marital deduction equal to the amount of property passing to the spouse in a qualifying manner. I.R.C. § 2056.

[64] MISS. CODE ANN. § 27-9-9 (1972).

[65] MISS. CODE ANN. § 27-9-11 (Supp. 1980).

[66] MISS. CODE ANN. § 27-9-15 (1972).

[67] MISS. CODE ANN. §§ 27-9-9-11, 15 (Supp. 1980).

[68] MISS. CODE ANN. § 27-9-5 (Supp. 1980).

[69] I.R.C. § 2056.

[70] I.R.C. § 2042.

[71] I.R.C. § 2511.

[72] I.R.C. § 2055.

CHAPTER FIVE

WILLS AND ADMINISTRATION OF ESTATES

Probate of a will and administration of an estate are the legal processes by which an estate is settled and distributed to the heirs. During the period of administration, the deceased person's assets are collected, debts and taxes are paid, and any remaining assets are distributed in accordance with his will. Essential to this process is a carefully drafted will.

A. *A will permits the maker, known as the testator,*[1] *to designate the persons and/or institutions to whom he wants his property to pass at his death.* If a person dies without a will, Mississippi law, referred to as the law of intestate succession, determines who receives the deceased person's property. Under the laws of intestate succession, a deceased person's children and spouse take the person's property in equal shares. If the deceased person has no spouse or children, the law designates which relatives will inherit his property.[2] Such a distribution may prove unsound. For example, the probate estate of a husband who dies without a will and is survived by a wife and three children will be divided among the wife and children in four equal shares. This result may cause the husband's estate to be burdened with unnecessary estate taxes due to the failure of the husband to fully utilize the estate tax marital deduction.[3] Further, property may pass directly to minors who are not legally able to deal with the property, requiring the appointment of a guardian by the court. These adverse consequences could be avoided by the execution of a will, leaving the spouse sufficient property to obtain the maximum marital deduction for the estate and creating trusts to manage the property of the minors or other persons not capable of properly managing their estates.

B. *The testator may waive certain probate and administration costs in a properly-executed will.* State law requires the executor or administrator (the representative of the estate) to post a bond with the court equal to the value of the decedent's estate, not including realty. He must also file an inventory and appraisal of certain assets of the estate. By means of a will, a testator may waive the legal requirements of inventory, appraisal[4] and bond.[5] Unless these requirements are waived, unnecessary court costs will be generated by the probate procedure, thereby reducing the assets passing to the heirs.[6]

C. *The testator may select his fiduciary representatives.* A testator may name his executor, who is the person or institution legally authorized to carry out the provisions of his will. The Executor will receive, for his services, a fee of 1-7% of the value of the estate assets handled by him, as determined by the court. If a decedent fails to name an executor, the court will appoint someone to serve.[7] By means of a will, a testator can also name a trustee to manage property passing to minors or other persons not capable of managing the property and a guardian for minor children or children under some other legal disability.[8]

D. *Certain tax advantages are available by means of a properly drawn will.* Although the estate tax marital deduction, discussed in Chapter 4, Estate and Gift Taxation, is available for property passing to a spouse in a qualified manner under a will or outside a will, the maximum tax savings of the marital deduction[9] may be lost without a properly drafted will. For example, the estate of a husband, survived by a wife and three children, may pay unnecessary estate taxes if the husband has no will. The wife receives only a one-fourth interest in the probate estate; whereas, the entire estate could have passed to the surviving spouse free of federal estate tax. Finally, an estate may lose the benefit of the estate tax marital deduction entirely if no will has been executed. If a husband and wife die simultaneously, state law prevents either spouse from inheriting property from the other; therefore, neither estate obtains a marital deduction. The spouse having the larger estate may provide in his will that he will be deemed to have predeceased the other spouse in case of a common disaster, thereby allowing a portion of his estate to qualify for the marital deduction.

EXECUTION OF A WILL

Of the three types of wills, the most common is an attested will. An attested will must be signed by the testator and two witnesses who sign in the testator's presence.[10] A holographic will must be entirely handwritten by the testator and signed by the testator at the bottom of the instrument. No witnesses are required.[11] A nuncupative will is made orally but is of very limited use. To make a valid nuncupative will, the testator must believe he is dying,[12] lack the ability and time to reduce the will to writing, and intend that his words constitute his will.[13]

In Mississippi, a will can be made by any person who is of sound and disposing mind and at least eighteen years of age.[14] A person is deemed to be of sound and disposing mind if he understands the significance of a will, knows the people who are to inherit his property and their relationship to him, and is capable of determining how he desires to dispose of his property.[15] The testator need only be of sound and disposing mind at the time he takes steps to execute a will. His lack of mental capacity before or after execution of the will does not raise a presumption that he is mentally incapable at the time the will is executed.[16]

Courts in other states have held that a retarded person may be of sound and disposing mind, possessing the capacity to execute a valid will, even though a guardian has been appointed for him.[17] Mental incompetency, thus, is not determinative of legal soundness for execution of a will.[18]

A will is not valid if the will was executed while the testator was under the undue influence of another person.[19] Undue influence will be presumed if suspicious circumstances surround the making of the will and if the testator has such confidence in a person or such a relationship with a person that the person exerts significant influence over the testator. Suspicious circumstances include cases in which the testator has a mental infirmity or a beneficiary is actively involved in the preparation or execution of the will.[20] Evident from the definition of undue influence is the need for the exercise of care by anyone assisting a retarded person in the execution of a will. Due to the difficult questions concerning the capacity of a retarded person and the possibility of undue influence, attorneys may be reluctant to prepare a will for a retarded person.[21]

A will clearly should be executed by any person, especially a parent, who is concerned about the future well-being of a retarded person. A will allows a parent to appoint a guardian for a retarded child even if the child is an adult,[22] and to create a trust for the retarded person's benefit. Such a testamentary trust will provide for the retarded person while avoiding an outright transfer to the beneficiary. The trust also affords the testator an opportunity to choose the person (i.e. the trustee) who will manage the trust property on behalf of the retarded person.

PROVISIONS FOR CHILDREN

A child may be disinherited if intentionally left out of a parent's will[23] or if bequeathed a nominal sum such as one dollar.[24] Such a child must have been living at the time the will was executed. A child born after execution of a parent's will inherits the share of his parent's estate that he would have inherited had the parent's property been distributed by intestate succession.[25] Such a child is referred to as an after-born or pretermitted child.[26]

Mississippi law further provides for a widow's allowance to be set aside from the assets of a decedent's estate.[27] The widow's allowance operates for the benefit of the decedent's widow[28] and children[29] whom the decedent was supporting at time of death and consists of the assets necessary to maintain and educate the qualified dependents for one year.[30]

The right to the one-year allowance is an absolute right[31] regardless of the condition of the estate.[32] Furthermore, this right is superior to liens of judgment creditors[33] but is inferior to certain preferred claims.[34] The amount of the allowance is within the discretion of the chancellor,[35] and the court may apportion the allowance, or any part thereof, according to the circumstances, ordering payment to the widow or any of the children.[36]

CLAIMS AGAINST THE ESTATE

A decedent's estate remains liable for valid claims of creditors against the decedent if the claims are probated[37] within 90 days of publication notice to creditors.[38] A claim is probated when registered with the Chancery Clerk[39] of the court which controls the administration of the decedent's estate.[40]

The creditor must present written evidence of the claim to the clerk, or if his claim is in the form of a judgment or a decree, he must present a certified copy thereof.[41] If there is no written evidence of the claim, then the creditor must submit either an itemized account or a statement of the claim.[42] If a claim is not properly probated within the time allowed, the creditor's claim is barred even if the executor was aware of the claim.[43] Claims against the estate may be contested by any executor or administrator, legatee, heir, or any creditor.[45]

After a claim has been properly probated and allowed, the executor or administrator of the decedent's estate has a duty to pay the claim from the assets of the decedent's estate.[46] Homestead property[47] and the widow's allowance, however, are considered to be exempt property and are not subject to debts of the decedent.[48]

Exempt from the claims of creditors is the first $30,000 in value of homestead property.[49] Homestead property consists of the widow's or widower's[50] place of residence and up to 160 acres of surrounding land.[51] Such property cannot be sold or divided into smaller lots for sale to pay the decedent's debts as long as the widow or widower continues to reside on the property and remains unmarried.[52]

If the decedent was a resident of a state institution, such as a retardation center, or the parent of such a person,[53] his estate may be liable for the costs of certain services provided by the institution during his lifetime. Claims against the estate of a retarded person or his parent for such costs should be filed in the same manner and within the same time period required for other claims, in order for the institution to obtain any reimbursement to which it is entitled.

SPECIAL CONSIDERATIONS FOR PARENTS OF A RETARDED CHILD

Drafting a will for a parent of a retarded child requires coordination of the parent's personal objectives for the child with his financial objectives for his estate. The age of the retarded child and the degree of independence and self-reliance that he has or may be expected to achieve will determine the manner in which property should be left to him. The size of the parent's estate, the number of other children or other persons to whom property will be left, estate tax considerations, and the amount of any government benefits received by the retarded child are considerations affecting the amount of property to be set aside for the benefit of the retarded child.

In many situations, the parent should name a testamentary guardian for the child in the event the child has no surviving parent. He should place any property to be held for the benefit of the child in a trust. More difficult questions, however, arise concerning the amount of property to be set aside for the child, the possible loss of certain government benefits and assistance to the child due to his inheritance of property, and the ability of a state institution providing care for the retarded child to reach the trust for reimbursement.

If a parent has a small estate, he may wish simply to leave his property to his surviving spouse, who will care for the child. In the event he has no surviving spouse, he may leave all his assets to his other children, omitting the retarded child and thereby preventing any loss of government benefits to the retarded child.

A parent having a larger estate, however, will want to secure the maximum estate tax savings possible for his estate while assuring adequate provision for the retarded child. Accordingly, the parent should be certain that his will is drafted to obtain the marital deduction[34] for bequests to a surviving spouse.

Property to be set aside for the retarded child should be placed in a trust, providing for discretionary distributions of income or corpus to or for the benefit of the child. The specific terms of such a trust must be determined by the parent's objectives after considering a number of factors. First, property passing to a retarded child may disqualify him for certain government benefits if such property is counted as an "asset" of the child.[55] Additionally, income from the trust paid to or for the child's benefit may constitute "unearned income," thereby reducing the amount of the child's monthly benefits from certain government assistance.[56] Finally, a state institution, such as a retardation center, may be able to attach a portion of the trust assets as reimbursement for care and services provided to the retarded child.[57]

A parent with substantial assets may not be concerned with these problems. He may wish simply to require the trustee to pay all amounts necessary for the proper care and support of such child; however, parents with insufficient assets, or those who simply wish to insure that the retarded child is adequately supported throughout his lifetime, should establish a trust that will supplement any benefits available to the child by means of federal or state assistance.[58] Such a trust should clearly state the parent's objective of supplementing governmental assistance to the child and should limit access to or attachment of the trust by creditors and/or governmental providers of services and benefits and the retarded child. Distributions from such a trust should be entirely discretionary with the trustee and could be limited to expenses for needs not otherwise provided for the child through government benefits or institutional care. Additionally, the trustee should be instructed to expend government benefits to which the child is entitled prior to invading the trust to pay for the care of the child, and he should be prohibited from expending trust funds for costs of care provided by governmental entities. The retarded child should have no direct access to the trust funds and should not receive income from the trust in excess of the "unearned income" limits placed on recipients of SSI benefits.

When creating such a trust, a parent should be aware that no court in Mississippi has considered the issue of the state's right of reimbursement against such a trust for the costs of care rendered to the retarded beneficiary;[39] however, since a parent can completely disinherit his retarded child, no public policy should be violated by the establishment of a trust which will provide additional care and services not available through government assistance.

The parent should name an appropriate trustee under the will to administer any trust created for a retarded child. Because of the special needs of the child, the appointment of co-trustees may achieve the best results. A bank or other financial institution can perform needed management and investment functions, while a family member, as co-trustee, can supervise the personal care of the child. Successor trustees may be named in the event the original trustees are unable to serve. For a small trust, designation of a family member as sole trustee may avoid certain administrative fees charged by banks and other corporate trustees. Additional administrative expense may be avoided if the parent waives bond and accounting requirements with respect to the named trustee, thereby eliminating court administration of the trust.

Two assets which may prove useful in funding a trust or providing support for a retarded child after the parent's death are life insurance proceeds payable at the death of the parent and pension benefits payable to the parent's survivors. These assets should be utilized in a manner compatible with the desired tax consequences, discussed more fully in Chapters 7 and 8.

FOOTNOTES

[1] "Testator" refers to a male that makes a will. A female who makes a will is known as a "testatrix." *BLACKS'S LAW DICTIONARY* 1323 (5th ed. 1979).

[2] MISS. CODE ANN. § 91-1-3 (1972).

[3] *See* Chapter 4, Estate and Gift Taxation at pp. 4, 13-14.

[4] Although no statutory authority exists for waiver of inventory and appraisal by a will, the court may dispense with these requirements for good cause shown. Unless waived, three appraisers must appraise and inventory the deceased person's property other than realty, debts owed the decedent and money. MISS. CODE ANN. § 91-7-109 (1972).

[5] MISS. CODE ANN. § 91-7-45 (1972).

[6] *See* MISS. CODE ANN. § 91-7-277 (1972) (annual accountings must be made to the court showing disbursements and receipts of the estate).

[7] The court will give preference to the spouse of the decedent, followed by other persons entitled to receive part of the estate. MISS. CODE ANN. § 91-7-63 (1972).

[8] MISS. CODE ANN. § 93-13-7 (Supp. 1979).

[9] *See* Chapter 4, Estate and Gift Taxation at pp. 4, 13-14.

[10] The signature requirement can be fulfilled if someone signs for the testator at the testator's express direction. MISS. CODE ANN. § 91-5-1 (1972).

[11] *Id.*

[12] MISS. CODE ANN. § 91-5-15 (1972).

[13] Sadler v. Sadler, 60 Miss. 251, 255 (1882).

[14] MISS. CODE ANN. § 91-5-1 (1972).

[15] Cowart v. Cowart, 211 Miss. 459, 462, 51 So.2d. 775, 776 (1951).

[16] *Id.*

[17] *See* Estate of Teel, 483 P.2d 603, 605 (Ariz. Ct. App. 1978); *see also* Thomas v. Hamlin, 404 S.W. 2d 569, 574 (Tenn. Ct. App. 1964); Estate of O'Loughlin, 183 N.W. 2d 133, 137 (Wis. 1971).

[18] Estate of Podgursky, 271 N.W. 2d 52, 57 (S.D. 1978).

[19] *See, e.g.*, Davion v. Williams, 352 So.2d 804, 806 (Miss. 1977).

[20] Croft v. Alder, 237 Miss. 713, 723-24, 115 So. 2d 683, 686 (1959).

[21] *See also*, In re Will of Moses, 227 So.2d 829, 838 (Miss. 1969) (holding attorney unduly influenced client who relied solely on attorney and with whom client had a personal relationship).

[22] MISS. CODE ANN. § 93-13-7 (Supp. 1980). The appointment of a testimentary guardian is ineffective if one parent is living. Campbell v. Mansfield, 104 Miss. 533, 547, 61 So. 593, 594 (1913).

[23] *See e.g.*, Guion v. Guion, 232 Miss. 647, 659-60, 100 So. 2d 351, 357 (1958).

[24] *See e.g.*, Cowart v. Cowart, 211 Miss. 459, 460, 51 So. 2d 775 (1951).

[25] These children fall into four categories and, depending on the category, may inherit an intestate share immediately or only upon reaching age twenty-one, marrying or leaving children capable of inheriting. MISS. CODE ANN. § 91-5-3, -5 (1972).

[26] *See* Mahaffey v. First Nat'l Bank, 231 Miss. 798, 826, 97 So. 2d 756, 767-68 (1957).

[27] MISS. CODE ANN. § 91-7-117 (1972).

[28] There is no such provision for a widower in Mississippi.

[29] The statute does not expressly limit the widow's allowance to the decedent's minor children; however, the statute permits a support allowance only for a deceased mother's infant children whom she was supporting. MISS. CODE ANN. § 91-7-135 (1972).

[30] *Id.*

[31] Howell v. Woody, 206 Miss. 863, 867, 41 So. 2d 35, 36 (1949); *cf.* Rush v. Rush, 360 So. 2d 1240, 1244 (Miss. 1978) (widow entitled to allowance regardless of will unless it appears that provisions therein are in lieu of the allowance). *But see* Best's Will v. Brewer, 236 Miss. 359, 363-64, 111 So. 2d 262, 263-64 (1959) (widow not entitled to allowance where husband and wife had executed a property settlement and he was no longer obligated to support her); Byars v. Gholson, 147 Miss. 460, 465, 112 So. 578-79 (1927) (wife living apart from husband without his fault and not being supported by him is not entitled to one year's support).

[32] *E.g.*, Thomas v. Bailey, 375 So. 2d 1049, 1054 (Miss. 1979) (right to widow's allowance is absolute regardless of whether estate is solvent or insolvent, and there is no time limitation in which allowance has to be requested so long as a final decree regarding the distribution of assets or the closing of the estate has not been rendered); Turner v. Turner, 30 Miss. 428, 431 (1855) (widow entitled to one year's allowance whether decedent dies testate or intestate and also regardless of whether estate is solvent or insolvent).

[33] *E.g.*, Thomas v. Bailey, 375 So. 2d 1049, 1054 (Miss. 1979); First National Bank of Commerce v. Donald, 112 Miss. 681, 691, 73 So. 723, 725 (1917).

[34] Mills v. Mills, 279 So. 2d 917, 926 (Miss. 1973) (allowance to widow and children in insolvent estates are inferior only to preferred claims involving expenses of last illness, funeral expenses, and costs of administration).

[35] Beckett v. Howorth, 237 Miss. 464, 469, 115 So. 2d 46, 48 (1959) (one year allowance is within chancellor's discretion); Moseley v. Harper, 202 Miss. 442, 444, 32 So.2d 192, 193 (1947) (appraiser's allowance is merely advisory, not binding).

[36] MISS. CODE ANN. § 91-7-141 (1972).

[37] MISS. CODE ANN. § 91-7-155 (1972); *See generally id.* § 91-7-145-155, 161 -167 (1972 & Supp. 1980).

[38] MISS. CODE ANN. § 91-7-151 (1972).

[39] MISS. CODE ANN. § 91-7-149 (1972).

[40] MISS. CODE ANN. § 91-7-151 (1972).

[41]MISS. CODE ANN. § 91-7-149 (1972). *See* Stewart v. Estate of Williamson, 243 Miss. 450, 455, 138 So. 2d 742, 744 (1961) (disallowing claim against estate which was based upon note executed by decedent because the original was not filed); Levy v. Merchants Bank and Trust Co., 124 Miss. 325, 329, 86 So. 807, 808 (1920) (holding alleged deed of trust insufficient to support account and stating that if a note is alleged to be in existence it must be probated.

[42]MISS. CODE ANN. § 91-7-149 (1972). *See* Johnson v. Hannon, 211 Miss. 207, 210, 213-14, 51 So. 2d 283, 285 (1951) (holding that claim for services rendered by attendant for "washing, ironing, cooking, cleaning house, nursing, caring for, serving as an attendant and servant, buying food and running errands, ministering while sick and weak from the infirmities of old age, lifting, bathing, and dressing decedent daily" for 842 days at $1 per day was sufficient to inform administrator that the services were rendered under implied, if not express, promise to pay, and claimant should be allowed to enter proof accordingly); Johnston v. Tomme, 199 Miss. 337, 343-45, 24 So. 2d 730, 730-31 (1946) (ruling that person who took paralytic into her home and cared for him for two and one-half years pursuant to an oral agreement that he would make his will in her favor by leaving her his entire estate and he actually did this, but later executed a new will leaving all his property to a nephew, was allowed to establish her claim quantum meruit). *But see* Johnson v. Odom, 202 Miss. 213, 218, 31 So. 2d 120, 121 (1947) (claim for "personal services" rendered held to be too broad and indefinite for administrator to determine whether or not it should be paid).

[43]MISS. CODE ANN. § 91-7-151 (1972) (Supp. 1980). It should also be noted that if the claim is registered, probated and allowed by the clerk and the affidavit is made in good faith but is defective, then the affidavit will be allowed to be amended, and the claim will be treated as if the affidavit were correct from the outset.

[44]MISS. CODE ANN. § 91-7-165 (1972).

[45]MISS. CODE ANN. § 91-7-165 (1972). *E.g.*, Wooley v. Wooley, 194 Miss. 751, 755, 12 So. 2d 539, 540 (1943) (if administrator objects to claim, the burden of proving the claim is on claimant even though it has been admitted for probate).

[46]MISS. CODE ANN. § 91-7-155 (1972).

[47]MISS. CODE ANN. § 91-1-23 (1972).

[48]MISS. CODE ANN. § 91-7-117 (1972).

[49] MISS CODE ANN. § 85-3-35 (Supp. 1980).

[50] Widowers as well as widows are eligible for the homestead exemption. MISS. CODE ANN. § 91-1-23 (1972).

[51] MISS. CODE ANN. § 85-3-35 (Supp. 1980).

[52] *Id.*

[53] See Chapter 2, Support of the Retarded Child-Family Assistance, at pp. 16-20, concerning the liability of a parent to support a retarded child.

[54] See Chapter 4, Estate and Gift Taxation, at pp. 4, 13-14.

[55] See Chapter 1, Support of the Retarded Child-Government Assistance.

[56] *Id.*

[57] See Chapter 2, Support of the Retarded Child-Family Assistance, at pp. 22-24.

[58] *See* Appendix A.

[59] *See* Chapter 2, Support of the Retarded Child-Family Assistance, at pp. 22-24.

CHAPTER SIX
TRUSTS

A trust is perhaps the most useful and flexible estate planning tool available.

(1) *What is a trust?*

A trust is a fiduciary relationship in which one party, the trustee, holds the property for the benefit of another person, the beneficiary.[1]

2) *What are the elements of a trust?*

(a)	*Grantor*-	The person who creates the trust.
(b)	*Trustee*-	The person who holds the trust property for the beneficiary according to the provisions of the trust.
(c)	*Beneficiary*-	The person for whose benefit the corpus is held. There are two types of beneficiaries: (1) income and (2) remainderman.
(d)	*Corpus or Res*-	The assets that are held by the trustee for the beneficiary.
(e)	*Trust instrument*-	The document which sets forth the rights, duties, and interests of the parties.[2]

(3) *Who can be a trustee?*

Generally, any natural person or corporation that is capable of taking title to the corpus may be the trustee. Government or municipal corporations, trust companies, banks, as well as individuals may function as trustees.

The sole beneficiary of a trust, however, cannot be the sole trustee because the legal and equitable titles would then merge.[3]

(4) *Who may be a beneficiary?*

Any legal entity or person that is capable of holding title to property and of being an obligee may be a beneficiary.[4]

(5) *Capacity to be a beneficiary:*

Basically, a minor, insane, or retarded person has capacity to be the beneficiary of a trust. A person who has the capacity to hold title to property may be the beneficiary. It does not matter that the beneficiary cannot transfer property or make a contract due to his or her disability.[5]

(6) *Income Beneficiary:*

An income beneficiary is one who is entitled to the income that results from the trust property, i.e. interest earned. Income beneficiaries typically receive income for their life, and upon their death, the principal passes to another.[6]

Remainderman:

A remainderman is one who is entitled to the remainder of the trust. In other words, this is a person who gets what is left over after the income beneficiaries die or their interest expires.[7]

For instance, if A creates a trust with income to B for life and remainder to C, B is an income beneficiary and C is the remainderman.

(7) *Living Trusts v. Testamentary Trusts:*

A living trust is one that is created during one's lifetime. It can be either a revocable or irrevocable trust.[8] On the other hand, a testamentary trust is created by one's will and takes effect at the grantor's death. Because of its nature, a testamentary trust is always irrevocable.[9]

The primary significance between a living trust and a testamentary trust bears upon the creation of the trust.[10] To create a testamentary trust, one must execute a valid will.[11] A living trust, however, is created by a valid gift, contract, or the exercise of a general power of appointment during one's lifetime.[12]

(8) *Revocable Trusts v. Irrevocable Trusts:*

The distinction between revocable and irrevocable trusts is applicable only to living trusts because testamentary trusts are always irrevocable.

Revocable Trusts:

Generally, the grantor transfers assets to the trustee but retains the power to revoke, alter, or amend the trust. He may also retain the right to the trust income during his lifetime. Upon the death of the grantor, the assets are either distributed or held in trust for another beneficiary.[13] Because the grantor reserves the right to change the trust or to receive the income from the trust, the corpus of the trust is included in the grantor's estate for estate tax purposes.[14]

Irrevocable Trusts:

An irrevocable trust is simply a trust that may not be revoked or changed after its creation.[15] As long as the grantor has not retained any beneficial trusts in the trust or has not given up such an interest within three years of death, the assets should not be included in the taxable estate of the grantor.[16] A gift tax may, however, be included on the creation of an irrevocable trust.[17]

(9) *What are the powers of a trustee?*

There are several different types of powers that a trustee might have, such as:

(a) *express*—these are powers that are specifically stated in the trust agreement, or by court order, or by statute.[18] Express powers generally include the power to sell the trust property, to invest the proceeds thereof, to pay income to beneficiaries and so forth.[19]

(b) *implied*—includes those powers that are essential in order to fulfill the purposes of the trust.[20]

(c) *mandatory*—the grantor may instruct the trustee to carry our certain administrative acts. In doing so, a power is created, and a duty to use the power is imposed upon the trustee.[21]

(d) *discretionary*—a discretionary power is one in which the grantor allows the trustee to use its judgment as to whether a certain act should be performed. It should be noted that even if the trustee has discretionary powers, the use of these powers is still within the purview of the courts. The courts generally, however, will not interfere with the trustee's decisions provided that the power is exercised in good faith after considering the various factors involved. On the other hand, the courts may instruct the trustee to change or reconsider the decision if he has acted in bad faith or arbitrarily.[22]

A typical power is the power to sell the assets. This power is either express or implied due to an inference to make the trust productive. As a natural consequence of a power to sell, the trustee is also given the power to execute contracts in relation to the sale.[23]

Other powers of the trustee include the power to incur expenses,[24] lease trust property,[25] mortgage or borrow money,[26] compromise, arbitrate, or abandon claims,[27] and exercise the powers of stockholders, including the power to vote.[28]

(10) *Co-Trustees and their Powers:*

Co-trustees exist when the grantor names two or more trustees of a private trust, and assuming he does not indicate otherwise, the powers are held jointly by all of the trustees. Accordingly, the trustees must all concur in the exercise of their powers. The co-trustees likewise hold the trust property as joint tenants.[29]

If one co-trustee tries to act without the others, his actions will generally be deemed void; however, the creator may allow a majority of three or more co-trustees to make decisions concerning the trust.[30] Furthermore, the grantor may give one power to one co-trustee and a different power to another co-trustee.

Unlike the situation of a private trust, co-trustees for a charitable trust are generally not required to have unanimity in order to act for the trust. Instead, a majority of the co-trustees may make decisions for the trust.[31]

(11) *Duties of the Trustee:*

The trustee must generally perform its duties with ordinary care unless stated otherwise in the trust instrument. In other words, the trustee must use the skills of an ordinary capable person.[32] Some of the more common duties are as follows:

(a) *Duty of Loyalty*—This is one of the most important duties of a trustee. The duty essentially requires the trustee to administer the trust in the best interest of the beneficiary and not let a third party's interest or the trustee's own interest interfere with the administration of the trust.[33]

(b) *Duty of Administration*—The trustee is under a duty to administer the trust upon his/her acceptance of the trust.[34] This duty is required even though the trustee may not receive any compensation for his/her services.[35]

(c) *Duty to Account*—Under this duty, the trustee is required to keep and render accurate accounts with respect to the financial condition of the trust.[36] Failure to keep accurate accounts makes the trustee liable for any loss or expenses resulting from this failure.[37] Furthermore, the trustee may be compelled by the beneficiary to produce an account of the trust to a court.[38]

(d) *Duty to Inform*—Similar to the duty to account, the trustee must furnish the beneficiary complete information upon his or her request. The trustee must also permit the beneficiary or a person authorized by the beneficiary to inspect the trust property.[39]

(e) *Duty to Make Productive*—This duty is either expressed or implied upon the trustee in most trusts.[40] Normally, the duty to make productive includes determining what funds are available for investment, when investments should be made, and what should be done in leasing or managing land.[41]

(f) *Duty to Earmark*—Basically the trustee has a duty to separate trust property from all other property and to earmark (label) all trust property as such. The duty to separate seeks to prevent the trustee from co-mingling trust funds with its own.[42] The duty to earmark essentially requires the trustee to mark bonds and notes as being held by him as trustee.[43]

(g) *Duty Not to Delegate*—This duty prohibits the trustee from delegating to others those acts that he can reasonably perform. It can, however, delegate certain acts.[44] To determine which acts may be delegated, the trustee should consider the following factors:

(1) amount of discretion involved;
(2) value and character of property involved;
(3) whether the property is principal or income;
(4) remoteness or proximity of the subject matter of the trust;
(5) if the act requires professional skills or facilities that the trustee may or may not possess.[45]

(h) *Duty of Impartiality*—If there are two or more beneficiaries of a trust, the trustee must deal impartially with them.[46] The trustee may, however, have the discretion to favor one beneficiary over the other under the trust provisions.[47]

(12) *How is a Trustee Selected?*

The grantor normally selects the trustee. In order to do so, the grantor only needs to show that a trust is in existence and that someone is desired to administer it. A trust, however, will not fail merely because the grantor does not select a trustee. The court will appoint a trustee in these situations and also in those situations where the named trustee is unable to administer the trust due to incompetency, disqualification, death, or refusing to accept the trust, but the grantor may provide for a substitute trustee or give the power to others to name a trustee at the outset in the trust.[48]

A "personal trustee' is one named by the grantor because he believes that trustee to be the *only* person who can administer the trust. This situation occurs primarily in family circumstances wherein the trustee is a family member. It should be noted that a substitute trustee will not be allowed if the personal trustee is unable to administer the trust.[49]

(13) *Compensation of the Trustee:*

A trustee has a right to be compensated for his services unless he has agreed to serve as trustee without charge. In order for the trustee to receive compensation, it is not necessary that it be expressly provided for in the trust instrument. If the instrument fails to create a provision for compensation, the trustee will be awarded a reasonable fee for his services either in equity or by statute.[50] If the trust is administered by co-trustees, the total compensation due is divided among them according to the services each has performed.[51]

A court of equity will award the trustee a reasonable fee for his services. In doing so, the court will consider the time and effort involved, special skills that the trustee used, the market rates for similar work, the success or failure of the trust, the amount of income and principal involved, the risk and responsibilities the trustee incurred, and other relevant factors.[52]

Many states, including Mississippi,[53] have statutes that provide for compensation to be awarded trustees. The statutes usually award compensation by establishing a fee schedule or a provision that provides that the trustee will receive reasonable compensation or such compensation as equity may determine to be fair. The rates are generally graduated so that a higher percentage is charged for smaller trusts.[54]

It should be mentioned that a trustee may lose his right to compensation if he waives this right. Also, the court may lower or refuse the trustee his compensation if he is guilty of a serious breach of trust.[55]

(14) *What is a Discretionary Trust?*

If the terms of the trust provide that the trustee shall pay to or apply for the beneficiary only so much of the trust income or principal for a certain purpose as he sees necessary, a discretionary trust exists.[56] The remainder of the trust income or property may be used for another purpose.[57] The name of this type of trust derives from the fact that the trustee acts in his discretion.[58] He can give the beneficiary some benefits or nothing at all.[59]

Another characteristic of a discretionary trust is that, prior to an election to pay or apply, a creditor or transferee of the beneficiary cannot compel the trustee to pay or apply.[60] If there is a suit to force the trustee to pay or apply, the trustee may maintain that he has chosen not to do so.[61] Accordingly, the beneficiary does not have an assignable interest or an interest subject to the claims of his creditors prior to the election by the trustee because of the very nature of the trust.[62] Once the trustee makes an election, however, the beneficiary has an interest that is assignable and subject to the claims of his creditors.[63]

It is worth noting that if the beneficiary assigns any interest or if his creditors endeavor to reach the trust before the trustee has made an election, the trustee will subsequently be liable to the assignee or creditor for the amount he paid or applied to the beneficiary.[64]

(15) *Spendthrift Trusts:*

A spendthrift trust is a trust which prevents the beneficiary from transferring his rights to future payments, and it also prevents his creditors from subjecting the beneficiary's interest to their claims.[65] Spendthrift trusts are created in an effort to provide for the support of someone but to also withhold the corpus or income from that person's lack of thriftiness.[66] Such a trust is not created for the purpose of preventing the beneficiary from spending the money after the trustee has given it to him or for the purpose of preventing his creditors from taking it thereafter.[67] Instead, the purpose of these trusts is to "prevent anticipation of trust income or principal by assignments of the right to receive future income or principal or from attempts by creditors of the beneficiary to reach such right."[68] In short, a spendthrift clause gives a beneficiary a right to future income, but he cannot assign this right or apply it as payment of his debts. Most states allow spendthrift trusts, although a few do not. In those states that allow them, some have placed statutory restrictions upon the trusts.[69]

Mississippi has upheld spendthrift trusts for beneficiaries[70] but not for grantors.[71]

INCOME TAXATION OF TRUSTS

For income tax purposes, a trust is treated as a separate entity.[72] The beneficiaries are generally taxed for the trust income that is distributed to them, and the trust is taxed for that which is not distributed to beneficiaries.[73] A trust is basically subject to the same income tax rates that apply to married persons filing separate tax returns.[74] The gross income of a trust is determined in the same way as that of an individual.[75] The law does, however, specifically state that the gross income of a trust includes:

(1) income accumulated for the unborn or unascertained persons or persons with contingent interests, and income held for future distribution;

(2) income to be distributed currently by the trustee or income collected by a guardian to be held or distributed as a court may direct;

(3) income received by estates during the period of administration;

(4) income which may be either distributed or accumulated according to the trustee's discretion.[76]

As a general rule, a trust is allowed the same deduction and credits as an individual.[77] There are, however, some differences. For instance, instead of having personal exemptions, a $300 deduction is allowed for simple trusts and a $100 deduction for complex trusts.[78] The taxpayer is also allowed credits, capital gains benefits, exclusions, etc.[79] Also, unlike individuals, trusts are allowed unlimited deductions for contributions to charitable organizations.[80] But, on the other hand, a trust is not allowed the credit for political contributions.[81] The trustee is required to make and file the return for the trust. He must also pay the tax on it.[82]

Both simple and complex trusts are allowed an additional deduction for distributions to beneficiaries.[83] The deduction is, however, limited by the trust's distributable net income (D.N.I.).[84]

Basically, in a simple trust, the beneficiaries must include in their gross income "the lesser of the trust income required to be distributed to them and the trust's distributable net income."[85] The amounts included in the beneficiaries' gross income have the same character as they did when in the hands of the trust.[86] For instance, if it was rent income for the trust, it is also rent income for the beneficiary.[87] Under I.R.S. §652, the trust is essentially treated like a conduit, and, thus, the amounts to be included in the beneficiaries' gross income are treated “as consisting of the same proportion of each class of items entering into distributable net income of the trust . . . as the total of each class bears to such distributable net income [illegible]”

According to the regulations, trust deductions are also allocated on the basis of the computation of D.N.I.[89] The regulations provide that (1) deductions directly attributable to one class of income must be allocated thereto;[90] (2) those not directly attributable to a specific class may be allocated to any item of D.N.I., but a certain portion must be allocated to tax exempt income.[91] This latter provision includes trustee's commissions, safe deposit box rent, and state income and personal property taxes.[92] If deductible items exceed their class, then they may be allocated to any other class of income,[93] however, excess deductions attributable to tax exempt income may not be allocated to other income classes.[94]

Complex trusts compute taxable income in essentially the same manner as simple trusts. Likewise, they share similar deductions. Furthermore, as in the case of a simple trust, the deduction for a complex trust may not exceed the D.N.I.[95] Unlike simple trusts, however, a complex trust may deduct any amount of gross income that is designated for charity.[96] Another characteristic of complex trust deductions is what is known as the tier system,[97] which determines what beneficiaries must include in their gross income.[98] Generally, the beneficiaries must include the amounts required to be distributed currently along with the amounts properly paid, credited, or required to be distributed to them.[99]

GRANTOR TRUST RULES[100]

Grantor trusts are trusts in which the grantor or nonadverse party "retains control over the income or corpus, or both, to such an extent that such grantor will be treated as the owner of the property and its income for income tax purposes."[101] A nonadverse party is any person who does not have "a substantial beneficial interest in the trust which would be adversely affected by the exercise or nonexercise of the power which he possesses respecting the trust."[102] As a result, the grantor is taxed on the income from the grantor trust, as owner, even though the beneficiary actually receives it. Consequently, the application of these rules requires that the separate existence of the trust for income tax purposes be ignored where the grantor possesses certain rights over the income or corpus of the trust.[103] Consequently, the normal income tax provisions for trusts discussed above do not apply when the grantor trust rules are applicable.

Since the grantor or nonadverse party continues to exercise authority and control over the trust, the code regards the grantor as owner of that part of the trust for income tax purposes. In addition, there is a possibility that the transfer of property in trust amounts to a gift equal to the value of the property transferred. In that case a gift tax may be payable by the grantor. If the gift is incomplete, it is likely that upon the grantor's death the trust corpus and any accumulated trust income will be included in his gross estate for estate tax purposes; therefore, when a grantor trust is created, the grantor should be aware of the various tax consequences.

The results reached through the application of these rules vary according to the powers or interest vested in the grantor and/or trustee, and also according to who is appointed by the grantor as trustee. Generally, the trust created by the grantor is either a nondiscretionary trust, a limited discretionary trust, or a totally discretionary trust. A nondiscretionary trust is a trust in which the trustee makes mandatory payments from the trust as the trust instrument directs. The trustee is not allowed to distribute the trust income as he deems necessary. An example is a trust in which the trustee is required to pay all the income generated by the trust property to the trust beneficiary annually.

A limited discretionary trust and a totally discretionary trust are just what the words imply. A limited discretionary trust gives the trustee some say-so in determining when the trust income is to be distributed to the beneficiaries. A discretionary trust gives the trustee the right to distribute trust income only when it is deemed appropriate or necessary.

In creating a grantor trust, the grantor either names himself, a nonadverse party, or an adverse party as trustee. A bank is generally a nonadverse party and a beneficiary of the trust, other than the grantor, is an adverse party. An adverse party is a party who does not qualify as a nonadverse party. A nonadverse party was previously defined.

There are several powers or interests, if retained by the grantor or nonadverse party, which will cause the income from a trust to be taxed to the grantor as owner of that portion of the trust. The grantor is treated as owner of any portion of a trust, either income or corpus, which will reasonably be expected to revert to him within ten (10) years after the transfer of that property to the trust;[104] however, this provision is not applicable if the reversion, within those ten (10) years, is to take effect only upon the death of the income beneficiary.[105]

The grantor is also treated as owner of a trust he created if he has the power to control the beneficial enjoyment of the trust income or corpus. That is, one is treated as owner of that portion of the trust over which he or a nonadverse party retains the power to control its beneficial enjoyment without any adverse party approving or consenting to the disposition.[106] There are several exceptions to this rule that allow the grantor to retain certain powers without being treated as owner of that portion of the trust. Several of these exceptions are the power of the grantor to distribute income for the benefit of a dependent,[107] the power to determine who shall enjoy the income generated after the trust has been existing for 10 years,[108] or the power to withhold income during the disability of a beneficiary. For our purposes, the grantor will be treated as the owner of all the income generated from a trust if the grantor has the power to determine which beneficiary among several will receive the income.

It is further stated in the Code that the grantor will be treated as owner of that portion of a trust over which he possesses certain administrative powers.[109] If the grantor has the power to deal with or dispose of the trust income or corpus for less than adequate and full consideration, or if he possesses the power to borrow the income or corpus of the trust without adequate security and without adequate interest, he is considered the owner of that portion of the trust. But the grantor will not be treated as the owner of any portion of the trust in which he exercises the above administrative powers if the grantor first gets the consent or approval of an adverse party before he exercises his administrative powers.

Generally, the grantor is treated as the owner of that portion of a trust over which he or a nonadverse party retains the power to revoke, amend, alter, or terminate without the consent or approval of an adverse party. So, if title to the trust property vests in the grantor upon the exercise of one of the above powers, the grantor will be treated as owner of that portion of the trust regardless of which power he possesses.[110]

The last grantor rule to be discussed treats the grantor as owner of that portion of a trust from which any income is used for the benefit of the grantor.[111]

This rule only applies if the grantor benefits from the income without the approval or consent of an adverse party or if the grantor or nonadverse party can apply the income at their discretion to benefit the grantor. Income is used for the grantor's benefit if it is actually or constructively "distributed to the grantor or the grantor's spouse; held or accumulated for future distribution to the grantor or the grantor's spouse; or applied to the payment of premiums on policies of insurance on the life of the grantor or the grantor's spouse."[112] A constructive distribution to the grantor or his spouse occurs when the trust makes a payment on behalf of the grantor or his spouse to another in accordance with his or her direction, such as the payment of the grantor's rent. This situation applies regardless if the income is actually paid or not.[113]

This rule, however, further provides that the grantor is not treated as owner of certain support trusts. To qualify, the trust income must be distributed for the support or maintenance of a beneficiary of the grantor, such as a child but not the grantor's spouse, whom the grantor or his spouse is legally obligated to support. So long as the grantor, in his capacity as the grantor, cannot use his discretion in determining when the payments are to be made, he will not be treated as owner of the entire trust. The fact that the grantor is also the trustee will not disqualify the grantor for purposes of this exception.[114] Generally, a support trust can be used for support purposes only, and payments from the trust can only be made after the grantor is unable to provide for the beneficiaries' support. Once a support payment is made, the grantor is treated as the owner of the income distributed or used for a support obligation of the grantor, and any income that is not distributed or used for such purposes is treated as being owned by the trust itself. For instance, if the trust earns $1,000 in interest income and the trustee uses $400 to pay a hospital bill of the beneficiary, who is the grantor's minor daughter and one whom the grantor is obligated to support, the grantor is treated as owner of the $400 used for support obligation and the remaining $600 is taxed to the trust if not distributed to the beneficiary.

There are other tax consequences which must be considered before a grantor trust is created. Gift and estate tax possibilities also must be weighed at the time the grantor trust is created. The mere fact that the grantor has transferred property in trust does not necessarily mean that one has removed their assets from his or her estate for estate tax purposes.

When an individual dies, his estate must pay estate taxes on the value of property owned at death. The value of the property included in the deceased individual's gross estate is its fair market value at the time of the decedent's death.[115] At the grantor's death, the gross estate will be increased by the value of any and all property over which he has retained an interest therein.[116] That includes any interest that the grantor has retained in property which he has transferred into a trust.

Some of those interests held by the grantor which will cause the trust property to be included in his gross estate are: "the possession of or enjoyment of, or right to the income from the property, or the right, either alone or in conjunction with any person to designate the person who shall possess or enjoy the income therefrom";[117] therefore, that portion of the grantor trust from which the grantor receives income or, as trustee, possesses a discretionary power over, is includable in his gross estate at the time of his death for estate tax purposes.

The grantor's gross estate is increased further by the value of any interest the grantor has in property transferred if the recipient of that property can only enjoy or possess the property by surviving the grantor and the grantor has retained a reversionary interest in the property.[118] The term "reversionary interest" means that if the recipient of the property does not survive, that is, outlive the grantor, then the property will revert or pass back to the grantor. This provision is seldom encountered in grantor trusts because the beneficiary of the grantor trust is not required to outlive the grantor and also the remainder interest is usually vested in an heir of the grantor.

If the grantor has retained the power to "alter, amend, revoke or terminate" a previous transfer of property, or "has released one of those powers within three years of his death," the value of the grantor's gross estate is increased by the value of the property over which he retained that power.[119] An example is where the grantor creates a trust and retains the power to revoke one-half of the transfer. As a result, his estate is increased by the value of one-half the trust property on his date of death.

The fact therefore, that the grantor has conveyed property into a trust does not necessarily exclude that property from the grantor's gross estate for estate tax purposes.[120] If the grantor wants to avoid paying estate taxes on property previously transferred, one must not retain any interest or powers in the transferred property, but if the grantor makes a complete transfer of property and does not retain any interest in the property transferred, he will pay a gift tax based on the value of the property conveyed. The value of the gift for gift tax purposes is the fair market value of the property at the time the transfer was made.[121]

Generally, if property is transferred so that it is not includable in the grantor's gross estate for estate tax purposes, then that transfer is subject to a gift tax. The gift tax applies to a transfer of property that is made to another individual, in trust, or otherwise. It applies to direct or indirect transfers of real or personal property. The transfer of property by the grantor into a trust, such as the assignment of an insurance policy or the conveyance of cash, may be a transfer subject to gift taxes.[122]

If the grantor/donor does not transfer his entire interest in the property by gift, but retains an interest therein, the gift tax is applicable to the interest transferred; however, if the value of the grantor's/donor's retained interest cannot be measured, the full value of the property transferred by gift is subject to gift taxes. In applying the gift tax to a transfer, donative intent on the part of the grantor is not an essential element[123].

The gift tax is not applicable to all transfers. The tax only applies to the transfer of a beneficial interest in property. The gift tax is not applicable if the transfer was made for full and adequate consideration in money or money's worth.[124] An illustration is one in which the grantor as donor transfers property by gift into a trust and retains the right to receive income for life. The trust instrument states that the grantor does not retain the power to revoke or change the beneficiaries, and upon the grantor's death, the principal is to be paid to the grantor's children. The interest payable to the grantor's children is a remainder interest, and since the children have a future interest in this property, the value of the remainder interest is subject to gift taxes at the time the transfer was made.[125]

A gift tax return is due in the year in which gifts to a donee total $10,000 or more. In computing the grantor's gift tax, the grantor is entitled to deduct $10,000 from the total value of gifts made during the year. Thus, for each donee of the grantor/donor, the donor excludes $10,000 from the value of the gift to determine the total amount of gifts for that year.[126] In the grantor trust situation, the trust beneficiary is considered the donee. If the grantor/donor makes a completed gift of $18,000 to the grantor trust and there is only one beneficiary or donee, the taxable amount of the gift for gift tax purposes is $8,000 ($18,000-10,000).

However, the value of a gift of a future interest does not qualify for the $10,000 exclusion even though the future interest is taxable for gift tax purposes.[127] A gift by the grantor to the trust which authorizes the trustee to make discretionary payments of trust income to the beneficiaries of the trust is an example of a gift of a future interest which does not qualify for the $10,000 exclusion. A remainder interest is another example of a future interest which is subject to gift taxes but does not qualify for the $10,000 annual per donee exclusion.

Under certain circumstances, a gift made by one spouse to a third person, someone other than his or her spouse, may for gift tax purposes amount to a gift with one-half the value of the gift being attributable to each spouse.[128] For this provision to apply, the spouse must be married and remain married during the year in which the gift was made. Also, each spouse must consent to the gift being made.[129] For example, if the husband transferred property as a gift into the trust giving the beneficiary a present interest in the property, and the value of the property is $20,000, and not a future interest, then only the husband will file a gift tax return, but no gift tax is owing on this transfer. The calculations are:

$20,000 gift by the husband to the grantor trust

$20,000 ÷ 2 (for gift tax purposes one-half is attributable to each spouse)

	$10,000	gift by the husband	$10,000	gift by the wife
less	10,000	per donee exclusion	10,000	per donee exclusion
	-0-	Value of gift subject to gift tax	-0-	Value of gift subject to gift tax

Only one gift tax return will be filed, and it is filed by the husband with the wife consenting to the gift.[130]

The following examples illustrate the application of the grantor trust rules, the estate tax rules, and the gift tax rules.

Example No. 1 - A Nondiscretionary Trust

The grantor transfers property into an irrevocable trust with the income payable to him for life and at his death the remainder is to be distributed to his disabled child or children in trust for their support and maintenance, or if none, to their heirs per stirpes. The grantor has no right to the trust corpus.

(a) The income received by the grantor from the trust during his lifetime is taxable to the grantor in the year received for income tax purposes.[131]

(b) For estate tax purposes, the value of the trust at the date of the grantor's death is includable in the grantor's gross estate because he has retained the right to income from the trust for life.[132]

(c) The value of the irrevocable remainder interest to the grantor's children is subject to gift tax at the time transfer was made, but the $10,000 per donee exclusion is not allowed as a deduction because it is a gift of a future interest.[133]

Example No. 2 - A Limited Discretionary Trust

Assume the same factual situation as in Example No. 1 except that the payment of income is subject to an ascertainable standard—health, education, maintenance, or support, and the trust can accumulate any income not distributed.

(a) All of the income earned by the trust is taxable to the grantor for income tax purposes. But if the trustee is an adverse party, such as a beneficiary of the trust but someone other than the grantor, the grantor may not be treated as the owner of the income not distributed to him. The trust may be treated as the owner of the accumulated income.[134]

(b) For estate tax purposes, the grantor's gross estate includes the value of the trust necessary for the support of the grantor during his life. It is quite possible that the value of the entire trust will be included in the grantor's gross estate.[135]

(c) A gift is made of the remainder interest. If the grantor proves that he will not require support from all of the trust property, then a gift equal to the value of the trust property not necessary for support is made and subject to gift tax.[136]

Example No. 3 - A Broad Discretionary Trust

Assume the same facts as in example No. 1 except that the trustee—any person other than the grantor—has the power to distribute income as it deems necessary. The trust is allowed to accumulate income.

(a) All the income generated will be attributed to the grantor for income tax purposes since the trust is not limited to support needs. If the trustee is an adverse party, the grantor may only be treated as owner of that income needed by him.[137]

(b) This trust should be excluded from the grantor's gross estate;[138] however, if a creditor is allowed to reach the corpus of the trust, the value of the trust property may be included in the grantor's gross estate because of the creditor's power to revoke the trust.[139]

(c) This transfer will normally constitute a completed gift and be subject to gift tax since the power to make distributions from the trust vests in a third person;[140] however, it may not be a complete gift to the extent it is used by the grantor.[141]

Example No. 4 - An Indirect Grantor Benefit Trust

The grantor transfers property into a trust stating that the income is payable to his disabled child as the trustee deems necessary for the child's support and maintenance. The undistributed income is to be accumulated and distributed with the remainder. The remainder is distributable to the heirs at law of the disabled child. The trust is irrevocable.

(a) Generally, the grantor is taxed on the income earned by the trust that can be used in the discretion of a nonadverse party to satisfy the legal obligations of the grantor, whether the income is distributed or not.[142] However, if the trust is obligated to support the grantor's dependents, and the discretion to make a distribution is possessed by the trustee, then the grantor is taxed only on the income that is actually distributed by the trust.[143] This advantage is the major one of a grantor trust. The income that is not distributed is taxed to the trust.

(b) The estate tax consequences are essentially unchanged. If the grantor is one of the trustees who possesses a discretionary power, even if there are many more trustees who have an adverse interest in the distribution, the value of the trust corpus will probably be included in the grantor's gross estate.[144] But if the grantor is not a trustee, none of the trust corpus is includable in his gross estate.[145] The grantor can name any competent person as trustee, other than himself, and achieve this result.

(c) In regard to gift taxes, there is no gift made on the transfer of property to the trust to the extent of the reasonable value of the property used to generate support income for the disabled child.[146] The burden of proof is on the grantor to show what portion of the income generated from the trust will be necessary to support the child. In that case, the present value of the remainder interest is taxable as a gift by the grantor at the time the property is transferred into the trust.

(d) In addition to the tax aspects, there are several advantages to creating a trust. By creating a trust, the grantor has provided a mechanism by which the child is to receive support after the grantor's death. The grantor will feel more comfortable knowing that his or her child will be provided for in the years following death. Since the child is unable to manage his own property, the trustee is able to manage the property for him. Once a grantor trust is created, it continues until the property is consumed or until the beneficiary dies or no longer needs the trust. Therefore, the grantor trust can provide financial security for a disabled child when it is most needed.

FOOTNOTES

[1] G. G. Bogert & G. T. Bogert, Handbook on the Law of Trusts § 1 (5th ed. 1973).

[2] *Id.*

[3] *Id.* at §30.

[4] *Id.* at §35.

[5] A. Scott, Abridgment of the Law of Trusts § 116 (1960).

[6] *See* Black's Law Dictionary 688 (5th ed. 1979) (definition of income beneficiary)

[7] *Id.* at 1162 (definition of remainderman).

[8] *Id.* at 1355 (definition of living trust).

[9] *Id.* at 1356 (definition of testamentary trust).

[10] *See* Bogert & Bogert, *supra* note 1, at § 22 (formality of the Wills Act).

[11] *See* Restatement (Second) of Trusts § 53 (1959) (must comply with Statute of Wills in order to create a testamentary trust).

[12] *See* Restatement (Second) of Trusts § 17 (1959) (discussion of various methods used to create trusts).

[13] J. Dukeminier & S. Johanson, Family Wealth Transations 409-10 (1972).

[14] I.R.C. § 2036-2038.

[15] *See* Black's Law Dictionary 1354 (5th ed. 1979).

[16] I.R.C. § 2035-2038.

[17] I.R.C. § 2511 (definition of irrevocable trusts).

[18] Mississippi has adopted the "Uniform Trustees' Powers Law." *See* MISS. CODE ANN. §§ 91-9-101-119 (1972).

[19] Bogert & Bogert, *supra* note 1, at § 88.

[20] *Id.*

[21] *Id.* at § 89.

[22] *Id.*

[23] *Id.* at § 133.

[24] Restatement (Second) of Trusts § 188 (1959).

[25] *Id.* at § 189.

[26] *Id.* at § 191.

[27] *Id.* at § 192.

[28] *Id.* at § 193.

[29] Bogert & Bogert, *supra* note 1, at § 91.

[30] Under Mississippi law if a power is vested in three or more trustees, the power may be exercised by a majority; however, a trustee who did not join in the exercise of that power is not liable to anyone, including the beneficiaries, for the consequences thereof. Likewise, a dissenting trustee, providing he has expressed his dissent in writing to any of the co-trustees to or during the joinder, is not liable for the consequences of an act that he joined at the direction of the majority. MISS. CODE ANN. § 91-9-113 (1972). Where two or more trustees are appointed to perform the trust, and if any of them do not accept the appointment or ceases to be a trustee after having been appointed as such, then the surviving or remaining trustees shall succeed to all powers, duties, and discretionary authority given to the trustees jointly and shall perform the trust accordingly. *Id.* It should be noted that this statute does not allow a co-trustee to escape liability for failing to participate in the trust administration or failing to attempt to prevent a breach of trust. *Id.*

[31] Bogert & Bogert, *supra* note 1, at § 91.

[32] *Id.* at § 93.

[33] *Id.* at § 95.

[34] Restatement (Second) of Trusts § 169 (1959).

[35] *Id.* §169, Comment b (1959).

[36] *Id.* §172 (1959).

[37] *Id.* §172, Comment b (1959).

[38] *Id.* §172, Comment c (1959).

[39] *Id.* §173 (1959).

[40] Bogert & Bogert, *supra* note 1, at § 101.

[41] Several states have adopted the so-called "prudent investor rule." *See* Bogert & Bogert, *supra* note 1, at § 106 (majority of states have adopted the rule either judicially or statutorily). In Mississippi, the prudent investor rule provides that the trustee is under a duty to "exercise the judgment and care" according to the circumstances "which men of prudence, discretion, and intelligence exercise in the management of their own affairs, not in regard to speculation, but in regard to the permanent disposition of their funds, considering the probable income as well as the probable safety of their capital." MISS. CODE ANN. § 91-13-3 (1972). Accordingly, the trustee is authorized to acquire and retain every kind of investment that men of prudence, discretion, and intelligence would acquire and retain for themselves. *Id.*

[42] Bogert & Bogert, *supra* note 1, at § 100.

[43] Restatement (Second) of Trusts § 179, Comment d (1959).

[44] *Id.* §171 (1959).

[45] *Id.* §171, Comment d (1959).

[46] *Id.* §183 (1959).

[47] *Id.* §183, Comment a (1959).

[48] Bogert & Bogert, *supra* note 1, at § 29.

[49] *Id.*

[50] *Id.* at § 144. MISS. CODE ANN. § 91-17-27 (1972) allows certain charges to be made against the income and principal. "One-half (½) of the trustees' regular compensation, whether based on a percentage of principal or income, and all expenses reasonable incurred for current management of principal and

application of income" may be charged against the income. *Id.* at (1) (e). Other charges that may be made against the income include "Court costs, attorney's fees, and other fees on other accountings or judicial proceedings if the matter primarily concerns the income interest. . .". *Id.* at (1) (d). On the other hand, those charges that may be made against the principal include "[t]rustee's compensation not chargeable to income under subsections (1) (d) and (1) (e), special compensation of trustees, expenses reasonably incurred in connection with principal, court costs and attorney's fees primarily concerning matters of principal, and trustee's compensation computed on principal as an acceptance, distribution, or termination fee." *Id.* at (3) (a).

Banks serve as trustees on a regular basis and usually have their own trust departments. A trust department generally offers a variety of services for trusts, wills, and estate administration. Compensation schedules from area banks for a trustee under agreement and under will are as follows:

(1) Jackson, Mississippi-ordinary services for personal property:

Minimum compensation	$500 annually
On the first $300,000	$7.50 per $1,000 value
On the next $700,000	$6.00 per $1,000 value
On the next $2,000,000	$3.50 per $1,000 value
On excess of $3,000,000	$2.50 per $1,000 value

If the trust assets are wholly invested in its Common Trust Fund, fees on the first $300,000 are $6.00 per $1,000 value and $5.00 per $1,000 value on the next $700,000. The minimum annual compensation is $300 in this situation.

Source: Deposit Guaranty National Bank (Jackson), *Personal Trust Services: Schedule of Compensation* (1980).

(2) Memphis, Tennessee-Annual administration charge:

Minimum Annual Administration Fee	$500
On the Principal:	
First $300,000	$4.50 per $1,000
Next $300,000	$3.25 per $1,000
Next $400,000	$2.50 per $1,000
Excess of $1,000,000	$1.90 per $1,000

On the Income:
- 6% of all income up to $25,000
- 4% of all income exceeding $25,000

Source: Union Planters National Bank of Memphis, *Fee Schedule for Personal Trusts* (1980). (Note: These fees are just a sample of a few of the trust related services of both banks and are not exhaustive by any means nor are they a comparison of the banks' fee schedules.)

[51] Bogert & Bogert, *supra* note 1, at § 144.

[52] *Id.*

[53] *See* note 46 *supra*.

[54] Bogert & Bogert, *supra* note 1, at § 144.

[55] *Id.*

[56] Restatement (Second) of Trusts § 155 (1959); Bogert & Bogert, *supra* note 1, at § 41.

[57] Bogert & Bogert, *supra* note 1, at § 41.

[58] *See* Restatement (Second) of Trusts at § 155 (trustee acts with uncontrolled discretion).

[59] *See* Bogert & Bogert, *supra* note 1, at § 41 (true discretionary trust grants trustee discretion to give beneficiary some benefits or give him nothing).

[60] *See* Restatement (Second) of Trusts at § 155 (1) (creditor cannot compel trustee to pay).

[61] Bogert & Bogert, *supra* note 1, at § 41. *See also* Restatement (Second) of Trusts at § 155, Comment (transferee or creditor cannot compel payment by trustee).

[62] Bogert & Bogert, *supra* note 1, at § 41. Furthermore, the nature of the trust prevents alienation and attachment. *Id.*

[63] *Id.* This is true only if the interest is not protected by a spendthrift clause. *Id.*

[64] Restatement (Second) of Trusts at § 155, Comments h-i, Illustrations 3-4; Bogert & Bogert, *supra* note 1, at § 41. The trustee is liable only if he had notice of the assignment or had been served with process by the creditor. Restatement (Second) of Trusts at § 155, Comments h-i, Illustrations 3-4; Bogert & Bogert, *supra* note 1, at § 41.

[65] Bogert & Bogert, *supra* note 1, at 40. *See* Restatement (second) of Trusts § 152 (1) (1959) (interest is not transferable and not subject to claims of creditors).

[66] *See* Bogert & Bogert, *supra* note 1 at § 40 (secure trust against person's improvidence for self-protection).

[67] *Id.*

[68] *Id.*

[69] *See* Bogert and Bogert, *supra* note 1, at § 150-154 (discussion of majority and minority views and applications).

[70] *E.g.*, Calhous v. Markow, 168 Miss. 556, 151 So. 547, 549 (1933) (holding that creditors could not reach corpus or income of spendthrift trust that gave beneficiary income and, at a certain age, the corpus); Mitchell v. Choctaw Bank, 107 Miss. 317, 65 So. 278, 279 (1914) (holding that a testamentary trust which named husband as trustee for children and giving him complete control over trust until children reached 21 did not vest, in the children, such an interest that could be subjected to creditor for payment of debt) Cady v. Lincoln, 100 Miss. 765, 57 So. 213, 216 (1912) (valid spendthrift clause in a will): Leigh v. Harrison, 69 Miss. 923, 11 So. 604, 607 (1892) (spendthrift trust of life income to son with remainder to trustee held valid against the creditors of the life beneficiary); *See* Annot., 119 A.L.R. 19, 56 (1939) (discussing that court upheld validity of the spendthrift trust in spite of statute providing that estates held in trust should be subject to the debts of the beneficiary as they would have been if such person had owned the like interest in the thing possessed as he may own in the uses or trusts thereof); MISS. CODE ANN. § 89-1-43 (1972) (trust estates subject to execution); *See generally* Annot., 34 A.L.R. 2d 1335, 1353 (1954) (rule that spendthrift trusts are valid is recognized in Mississippi); *See also* Carter v. Berry, 243 Miss. 321, 342-43, 354, 136 So. 2d 871, 875, 881 (1962) (trust containing spendthrift provision does not violate rule against perpetuities).

[71] Deposit Guar. National Bank v. Walter Heller & Co., 204 So. 2d 856, 859 (Miss. 1967) (holding that a spendthrift trust for benefit of the grantor is invalid even if there is a contingent remainder in third person).

[72] Commerce Clearing House, Federal Income Taxes of Decedents and Estates § 43 (1980).

[73] *See* G. G. Bogert & G. T. Bogert, The Law of Trusts and Trustees § 268 (2d ed. 1977).

[74] Commerce Clearing House, *supra* note 68, at § 43. Even though the same rates apply, separate rate tables must be used. *See* I.R.C. § 1 (e) (rates for estates and trusts). There are some differences, however, in credits and deductions. Commerce Clearing House, *supra* note 68, at § 43. Form 1041 is filed by a trust. *Id.*

[75] *Id.*

[76] I.R.C. § 641 (a) (1) - (4).

[77] [1980] 5 Stand. Fed. Tax Rep. (CCH) ¶ 3604A.

[78] I.R.C. § 642 (b). A simple trust is a trust that is required to distribute all trust income currently to the beneficiaries. On the other hand, a complex trust is any trust other than a simple trust. *See* J. Chommie, The Law of Federal Income Taxation 316 (1968) (definitions of simple and complex trusts).

[79] [1980] 5 Stand. Fed. Tax. Rep. (CCH) ¶ 3605.01.

[80] I.R.C. § 642 (c) (1).

[81] I.R.C. § 642 (a) (2).

[82] [1980] 5 Stand. Fed. Tax. Rep. (CCH) ¶ 3604B.

[83] J. Chommie, *supra* note 74, at 318.

[84] I.R.C. § 643 (a). Distributable net income is the taxable income of the estate or trust before deductions are allowed for distributions of income and personal exemption. *Id.*

[85] Bogert & Bogert, *supra* note 69, at § 266. Whether the income is required to be distributed depends on the trust and local law. *Id.*

[86] Treas. Reg. § 1. 652 (b) - 1.

[87] *Id.*

[88] Treas. Reg. § 1.665 (b)-2. *See* Bogert & Bogert, *supra* note 69, at § 266 (trust treated like conduit).

[89] I.R.C. § 652 (b).

[90] Treas. Reg. § 1.652 (b)-3 (a).

[91] Treas. Reg. § 1.652 (b)-3 (b). *See* Bogert & Bogert, *supra* note 69, at § 266 (pro rata portion).

[92] Treas. Reg. § 1.652 (b)-3 (c).

[93] Treas. Reg. § 1.652 (b)-3 (d).

[94] *Id.*

[95] Bogert & Bogert, *supra* note 69, at § 267.

[96] *See* Bogert & Bogert, *supra* note 69, at § 267 (deduct amounts paid or permanently set aside for charity).

[97] *See* J. Chommie, *supra* note 74, at § 31 (two-tier system characterizes amounts beneficiaries receive). Simply put, the first tier involves the amount of income for the taxable year that is required to be paid out currently, and the second tier includes any other amounts correctly paid, credited or required to be paid out for that taxable year. I.R.S. § 1.1661 (a)-2.

[98] Treas. Reg. § 1.662 (a)-1. For a discussion of the two-tier system, *see* Bogert & Bogert, *supra* note 69, § 267 at 482-84.

[99] *See* Bogert & Bogert, *supra* note 69, at § 268.5 (gross income of complex trusts).

[100] I.R.C. § 671-677.

[101] Black's Law Dictionary 630 (5th ed., 1979).

[102] I.R.C. § 672.

[103] I.R.C. § 671.

[104] I.R.C. § 673.

[105] *Id.*

[106] I.R.C. § 674 (a).

[107] I.R.C. § 674 (b) (1).

[108] I.R.C. § 674 (b) (2).

[109] I.R.C. § 675.

[110] I.R.C. § 675 (a).

[111] I.R.C. § 677 (a).

[112] I.R.C. § 677 (a), Treas. Reg. § 1.677 (a)-1.

[113] *Id.*

[114] I.R.C. § 677 (b), Treas. Reg. § 1.677 (b)-1.

[115] Treas. Reg. § 20.2031-1 (b).

[116] I.R.C. § 2031, 2033.

[117] I.R.C. § 2036 (a).

[118] I.R.C. § 2037.

[119] I.R.C. § 2038.

[120] I.R.C. § 2035.

[121] I.R.C. § 2512.

[122] I.R.C. § 2511.

[123] Treas. Reg. § 25.2511-1.

[124] *Id.*

[125] *Id.*

[126] I.R.C. § 2503.

[127] Treas. Reg. § 25.2503-3.

[128] I.R.C. § 2513.

[129] Treas. Reg. § 25.2513-1.

[130] *Id.*

[131] I.R.C. § 674 (a), 677 (a).

[132] I.R.C. § 2036 (a) (1).

[133] I.R.C. § 2511.

[134] I.R.C. § 674 (a), 677 (a).

[135] I.R.C. § 2036 (a).

[136] I.R.C. § 2511.

[137] I.R.C. § 674 (a), 677 (a).

[138] I.R.C. § 2036 (a).

[139] I.R.C. § 2038 (a)%

[140] I.R.C. § 2511.

[141] *Id.*

[142] I.R.C. § 674 (a).

[143] I.R.C. § 677 (b).

[144] I.R.C. § 2036, Treas. Reg. § 20.2036-1.

[145] Treas. Reg. § 20.2036-1.

[146] Treas. Reg. § 25.2511-1, 25.2511-2.

CHAPTER SEVEN
LIFE INSURANCE

Life insurance[1] can be very useful in planning an estate. It may be used to guarantee that the insured's family will have sufficient assets after the insured's death for support, medical expenses, and education where they otherwise would not. Life insurance may also be used to pay the estate taxes and administration expenses of the insured's estate and to provide living expenses for the insured's family until other assets can be sold.[2]

TYPES OF POLICIES

There are three main types of life insurance: whole life, term, and endowment.[3] A whole life policy remains in force so long as the premiums[4] are paid. If the policy is in force at the time of the insured's death, a death benefit in the amount of the face value of the policy is paid to the beneficiary.[5] A whole life policy also provides cash value which increases each year that the policy is in force and is payable to the policy owner if the policy lapses.[6] Limited pay life insurance is a form of whole life insurance which provides the same benefits as a whole life policy, but premiums are only paid for a stated period of time. Because the limited pay life policy is paid up within a specified time, the yearly premiums are greater than those for a whole life policy.[7] Term insurance is issued for a specified period, the term, and only provides benefits at the insured's death if then in force. The premiums are generally cheaper than for a whole life policy while the insured is young but increase as the insured grows older.[8] In an endowment insurance policy, a premium is paid for a stated period of time, but the premiums are higher than those for limited pay policies. The face amount of the policy is paid on either the expiration of the term or the prior death of the insured. Endowment policies are generally used to insure that there will be sufficient funds for education of children on the death of their parents.[9]

SETTLEMENT OPTIONS

Besides a lump sum settlement, there are four primary ways in which the proceeds of a life insurance policy may be paid to the beneficiary after the death of the insured: the interest option, the installment option, an annuity,[10] and special options. The beneficiary may select an option if the insured has not previously done so.[11]

Under the interest option, the beneficiary periodically receives interest on the insurance policy proceeds which are retained by the insurance company. At a specified time, the proceeds may be withdrawn by the beneficiary.[12]

There are two types of installment options: installments for a fixed amount and installments for a fixed period. Under a fixed amount option, the beneficiary periodically receives payments from the policy proceeds and interest until the proceeds and interest are exhausted. Under a fixed period option, the beneficiary receives payments from the policy proceeds and interest for a fixed period of time. The amount of each payment depends on the total number of payments to be made and the total amount to be distributed. Under either the fixed amount or fixed period option, the secondary beneficiary begins receiving any unpaid installments on the death of the primary beneficiary.[13]

There are two principle types of annuity options: straight life and joint and survivor. Under a straight life annuity option, insurance policy proceeds are used to buy an annuity which periodically pays the primary beneficiary a specified amount for life. The payments end on the death of the primary beneficiary. Each of two beneficiaries receive periodic payments until the death of the last survivor under a joint and survivor option.[14]

Special settlement options are sometimes available. This type of insurance allows a settlement to be fashioned from a combination of options that best meet the needs of the beneficiary.[15]

TAX CONSIDERATIONS

Premiums paid by a taxpayer for insurance policies on his life are not tax deductible.[16] Proceeds of insurance policies paid on the death of the insured are not taxable to the beneficiary,[17] but interest on the proceeds is taxable.[18] Dividends earned by a life insurance policy are deemed to be a return of premium and therefore are not taxable as income,[19] but the interest on dividends left with the insurance company is taxable.[20]

Estate taxes must be paid on life insurance on a taxpayer's life over which the taxpayer retained any power.[21] These powers are known as incidents of ownership[22] and include such powers as the ability to change beneficiaries or to assign the policy.[23] The amount subject to estate taxes if the taxpayer has retained any incidents of ownership over a policy is the face amount of the policy plus dividend accumulations and unearned premiums[24] but less any loans outstanding against the policy.[25] In order to escape estate tax liability on an insurance policy, the policy may be given away to an irrevocable insurance trust for the benefit of family members or to an individual directly, such as the named beneficiary of the policy. But gift tax liability may be incurred. Since the gift tax value is approximately equal to the cash surrender value of the policy, the gift tax liability incurred will still be less than the estate tax liability incurred if the policy is not given away.[26] If given away within three years of death, however, the policy is still includable in the taxpayer's estate.[27]

FOOTNOTES

[1] Life insurance is defined as a contract in which one party, the insured, pays a second party an amount based on such factors as the age and health of the insured. In return, the second party promises to pay an agreed upon sum of money to a named beneficiary should the insured die within the period covered by the policy. J. Angell, Fire and Life Insurance 296 (reprinted. 1972). Life insurance is primarily issued by two types of companies. A mutual company generally writes only policies that pay dividends and is owned by its policyholders. A stock company generally writes only policies which pay no dividends and is owned by its stockholders. A dividend is a distribution to policyholders of part of the insurance company's profits. R. Jackson, *Surplus and Dividends*, in Life and Health Insurance Handbook 184 (3rd ed. 1973).

[2] H. Weinstock, Planning An Estate § 10.1-.2 (1977).

[3] *Id.* at § 10.6.

[4] A premium is the periodic payment due the insurance company for an insurance policy. Beadles, *Protection Functions of Life and Health Insurance* in Life and Health Insurance Handbook 29 (3rd ed. 1973).

[5] The amount actually paid is the face amount of the policy plus accrued dividends but less any outstanding loans against the policy. Williams, *Contracts - Whole Life and Endowment*, in Life and Health Insurance Handbook 71 (3rd ed. 1973). For a further discussion of loans against the policy, *see* note 6 *infra*.

[6] The owner of a whole life insurance policy may, at any time, borrow part or all of the accumulated cash value. Such a loan may be very attractive in view of the fact that the interest rate on the loan is generally very low. This interest rate is specified in the policy contract. Accumulated cash value may also be used to purchase a paid up whole life insurance policy for a lesser face amount or to buy term insurance. H. Weinstock, *supra* note at § 10.8,.30.

[7] Williams, *Contracts - Whole Life and Endowment*, in Life and Health Insurance Handbook 66-73 (3rd ed. 1973).

[8] Beadles, *Contracts - Term Insurance*, in Life and Health Insurance Handbook 55, 63-64 (3rd ed. 1973).

[9] Williams, *Whole Life and Endowment*, in Life and Health Insurance Handbook 75-77 (3rd ed. 1973).

[10] For a further discussion of annuities, see Chapter Eight.

[11] H. Weinstock, *supra* note 2, at § 10.24 (1977).

[12] *Id.* at § 10.25.

[13] Lynn, Introduction to Estate Planning § 6.8 (2nd ed. 1978).

[14] *Id.*

[15] H. Weinstock, *supra* note 2 at § 10.28 (1977).

[16] Treas. Reg. § 1.262-1 (b) (1) (1958).

[17] I.R.C. § 101 (a) (1).

[18] I.R.C. § 101 (c). Taxable interest on an installment option is the amount that each periodic payment exceeds the prorated amount that could have been received as a tax free lump-sum. The lump-sum is prorated over the option payment period. I.R.C. § 101 (d) (1). Taxpayer who desires to receive installment payments from a matured endowment policy must make such an election within 60 days of maturity of the policy. Failure to make such an election within 60 days renders the taxpayer liable at maturity for the entire gain on the policy. If the election is made within 60 days, the annuity rules of taxation apply. I.R.C. § 72 (h). For the tax consequences of annuities, *see* Chapter Eight.

[19] Treas. Reg. § 1.101-6 (1957).

[20] No tax liability will be incurred if the policyholder elects to apply dividends against future premiums, thereby reducing the amount of future premiums due. [1981] Index Fed. Tax Rep. (CCH) § 205.04.

[21] I.R.C. § 2042 (2).

[22] *Id.*

[23] Other incidents of ownership include the right to surrender or cancel the policy, to revoke an assignment of the policy, or to pledge the policy as security for a loan. Treas. Reg. § 20.2042 (1) (c) (1958).

[24] The unearned premium is the total premium paid for a policy period multiplied by the fractional part of the period remaining. D. Cody & H. Boothroyal, *Group Premiums, Experience Rating, and Reserves,* in Life and Health Insurance Handbook 484 (3rd ed. 1973).

[25] J. Creedon, Some Uses of Life Insurance in Estate Planning 69 (1974). *See* Treas. Reg. § 20.2042-1 (a) (3) (1958).

[26] *H. Weinstock, supra* note 2 at § 10.18 (1977). The gift tax value of a paid up insurance policy is the replacement cost of the policy as of the date of the gift. Treas. Reg. § 25.2512-6 (a) (1958). The gift tax value of an insurance policy that is not paid up is the policy's interpolative terminal reserve value, approximately equal to the policy's cash surrender value, plus the unearned premium and accrued dividend but less any loans outstanding. L. Silverstein & G. Sherman, *Estate and Gift Taxation of Life Insurance*, in Life and Health Insurance Handbook 889 (3rd ed. 1973). *See* Treas. Reg. § 25.2512-6 (a) (1958) (valuation of insurance policies). The interpolative terminal reserve is the amount set aside annually by the insurance company so that there will be sufficient funds from which to pay the proceeds of the policy should the policyholder die. *H. Weinstock, supra* note 2 at § 10.17 (1977). Since the interpolative terminal reserve increases each year, there is less gift tax liability if the policy is given away in the early years of the policy's existence. J. Creedon, *supra* note 25, at 52-53 (1974). Term insurance has no interpolative terminal reserve. Since only the unearned premium is subject to gift tax, there is generally little or no gift tax liability when a term policy is given away. L. Silverstein & G. Sherman, *Estate and Gift Taxation of Life Insurance*, in Life and Health Insurance Handbook 889 (3rd ed. 1973).

[27] I.R.C. § 2035 includes in a taxpayer's estate the full value of an insurance policy given away within three years of the taxpayer's death.

CHAPTER EIGHT

ANNUITIES

An annuity is an agreement to make payments of a specified sum at periodic intervals for either a specific term or for as long as the annuitant lives.[1] Annuities, which are usually used to provide income for the annuitant when he or she grows old,[2] differ from life insurance which provides benefits at the death of the insured.[3]

TYPES OF ANNUITIES

Annuities fall into two broad categories: commercial and private. A commercial annuity is one that is sold by an organization such as an insurance company.[4] A private annuity is one paid by someone who ordinarily does not sell annuities. Private annuities usually result from interfamily transfers for estate planning purposes in exchange for a promise to make periodic payments to the transferor.[5] Private annuities will not be explained in detail since their use is restricted.

There are four principle types of commercial annuities: straight life, refund, joint life and survivorship, and life annuity with term certain.[6] A straight life annuity provides periodic payments for the life of the annuitant. Regardless of the amount paid, the payments terminate at the death of the annuitant.[7] For example, if A pays $12,000 for an annuity that is to pay him $100 per month but A dies 6 months after the payments begin, no further payments are made.

Under a refund annuity, the annuitant receives periodic payments until death. At death, the amount by which the purchase price of the annuity exceeds the total periodic payments made during life to the annuitant is refunded to the annuitant's beneficiary.[8] For example, if A pays $12,000 for an annuity that is to pay him $100 per month but A dies 10 months after the payments begin, $11,000 will be refunded. This refund can be made by continuing the periodic payments under an installment refund annuity or by making a lump sum refund under a cash refund annuity.[9]

A life annuity with a term certain provides the annuitant with periodic payments for life. If, however, the annuitant dies before the end of a specified term, payments are made to the annuitant's beneficiary for the remainder of the term.[10] For example, if A owns an annuity with a guaranteed term of 100 months but dies after receiving only 50 payments, the payments will continue to be made to A's beneficiary for the remaining 50 months of the term. If A lives for 150 months after the payments begin, the payments will continue until A's death and then cease.

A joint life and survivorship annuity provides periodic payments to two annuitants for their joint lives and continues for the survivor's life. This type of annuity is usually written on the lives of a husband and wife.[11] Payments during the life of the survivor may be reduced depending on the annuity.[12] For example, A and his wife, B, pay $12,000 for an annuity that is to pay them $100 per month while they both are living and $100 per month to the survivor after the death of either. This annuity could also be written so as to provide A and B with $110 per month while both are alive but only $80 per month to the survivor.

INCOME TAXATION OF ANNUITIES

The fractional part of each annuity payment that is not taxable as income is known as the exclusion ratio. The exclusion ratio equals the total amount paid for the annuity divided by the total expected return from the annuity.[13] If the annuity is to be paid for a specified term, the expected return equals the total number of payments to be made multiplied by the amount of each payment.[14] For example, A pays $10,000 for an annuity that is to pay $1,000 per year for 15 years. The expected return is $15,000 (15 x $1,000) and the exclusion ratio is 10,000/15,000 or 2/3. Therefore, A does not have to pay income tax on two-thirds of each $1,000 received each year from the annuity. If the annuity is to be paid for life, the total number of payments to be received is based on the life expectancy of the annuitant as derived from the life expectancy tables of the Treasury Department.[15] For example, A, a male, is to receive $100 per month ($1200 per year) for life from an annuity. At the time the payments are to start, A's age at his nearest birthday is 33. Under life expectancy Table I at Treas. Reg. section 1.72-9, A has a life expectancy of 40 years. His expected return from the annuity is therefore $48,000 (40 x $1200).

GIFT TAXATION OF ANNUITIES

The taxable value of a gift of an annuity that is purchased at the time of the gift is the cost of the annuity. If the annuity is given away at a date considerably later than the date of purchase, the gift tax value is the amount that would be charged for a single premium annuity providing the same annual payment for the life of a person of the donor's age.[16] For example, A purchases an annuity from company X and is to receive $1,000 per year for life from the annuity. When A is 40 years old and after receiving annuity payments for 5 years, A gives the annuity away. The gift tax value is the amount that company X would charge a 40 year old male for an annuity which will pay the purchaser $1,000 per year for life.

ESTATE TAXATION OF ANNUITIES

The present value of an annuity at the date of death will be includable in a taxpayer's estate if the taxpayer had a right to the annuity[18] or was in fact receiving payments from the annuity during life.[19] The present value of an annuity is the value at the taxpayer's death of the payments from the annuity that are payable to the taxpayer's beneficiary.[20] The Treasury Department has drawn up tables which give the present value of both life and term-of-years annuities.[21] For example, A owns an annuity that is to pay A $10,000 per year for the life of his brother, B. A dies when B is 52 years 8 months old and after A has received a payment. Under Table A (1) of section 20.2031-10 of the Treasury Regulations, 10.7200 is the figure in column 2 that is opposite 53, the number nearest B's actual age. The present value of the annuity at the date of A's death is therefore $107,200 ($10,000 x 10.7200). If, however, A's annuity is to pay $10,000 per year for 10 years and A dies after having received the fifth payment, A's beneficiary would be entitled to receive 5 more payments. Under Table B of section 20.2031-10 of the Treasury Regulations, the figure in column 2 opposite 5 years is 4.2124. The present value of the annuity is therefore $42,124 ($10,000 x 4.2124).

ANNUITIES UNDER QUALIFIED RETIREMENT PLANS

Certain types of plans, known as qualified retirement plans, provide annuities which are specifically excluded from the estate of the owner of the plan[22] but cannot be given away.[23] Such an annuity is not subject to estate taxes even though paid to the owner's spouse or children after the owner's death.[24] Additionally, the earnings derived from investing the contributions to a qualified plan are not taxable as income until the earnings are actually withdrawn from the plan.[25]

There are four primary types of qualified retirement plans: (1) defined contribution, (2) defined benefit, (3) HR-10 or Keogh, and (4) individual retirement account (IRA).[26] Defined contribution[27] and defined benefit retirement plans are the principle types of qualified corporate retirement plans.[28] In a defined contribution plan, a maximum of twenty-five (25%) of each participating employee's income[29] is contributed to the plan(s) by the company and invested.[30] The amount in the employee's account at the time of the employee's retirement[31] is used to buy an annuity for the employee or to make periodic or lump-sum payments to the employee.[32] A defined benefit plan guarantees the participating employee a specified amount of pension on retirement.[33] The employer periodically contributes the amount necessary to provide the promised pension.[34] Under both types of corporate pension plans, the company's contribution to the plan is tax deductible to the company[35] but not taxable as income to the employee when made.[36] While the annuity cannot be given away,[37] a beneficiary of the payments made after the employee's death can be named without incurring gift tax liability.[38]

The proceeds from a qualified corporate plan may be taken in a lump sum or in periodic installments.[39] If taken in periodic payments and only the employer has contributed to the plan, each payment is taxable as ordinary income when received by the employee.[40] If both the employer and employee have contributed to the plan, the periodic distributions are treated as an annuity for income tax purposes. The cost of the annuity is the amount contributed by the employee.[41] For example, both A, a male aged 65 at retirement, and A's employer contribute to a plan for A's benefit. A contributes $5,000 and is to receive $1,000 per year for life. Under life expectancy Table I at section 1.72-9 of the Treasury Regulations, A has a life expectancy of 15 years. His expected return from the annuity is $15,000 ($1,000 x 15) and the exclusion ratio[42] is $5,000/$15,000 or ⅓. Therefore, A does not have to pay income tax on one-third of each $1,000 annual payment from the annuity. If, however, the employee will recover his contribution to the plan within 3 years from the time the annuity payments begin, the payments are not taxable to the employee until his full contribution is recovered. Subsequent payments are then fully taxable as ordinary income;[43] therefore, if A in the previous example contributes $5,000 to the plan but is to receive $2,000 per year from the annuity, A would recover his $5,000 investment within three years. A pays no tax on the first two yearly payments and no tax on the first $1,000 received the third year. Since A has now recovered his $5,000 investment, the second $1,000 of the third yearly payment and all subsequent payments are taxable as ordinary income to A.

If the proceeds of the annuity are taken in a lump sum,[44] the employee may be entitled to treat part of the proceeds attributable to the employer's contribution as long-term capital gain[45] with the remainder treated as ordinary income.[46] An accountant or tax attorney should be consulted before making a withdrawal due to the complexity of the laws concerning lump sum payments from qualified retirement plans.[47]

Keogh and individual retirement accounts are the principle types of qualified individual retirement plans.[48] Any self-employed person[49] can contribute up to 15% of his annual income, not to exceed $15,000, to a Keogh plan.[50] For example, if A is self-employed and earns $10,000 in 1982, A can contribute up to $1,500 (15% of $10,000) in 1982 to a Keogh plan. If, however, A earns $100,000 in 1982, the maximum of $15,000 can be contributed to a Keogh plan. If the maximum $15,000 is contributed each year for 25 years to a Keogh plan that earns 8% interest, the account will contain $1,096,500 at the end of the 25 year period.[51] If the plan continues to earn 8% interest, over $100,000 per year can be withdrawn in retirement benefits for 25 years before the funds will be exhausted.[52]

For taxable years before 1982, if employed by a company with no qualified plan,[53] an employee may contribute up to the lesser of 15% of his annual salary or $1,500 to an IRA.[54] For example, if A works for a company that has no qualified plan and earns $8,000 in 1981, A can contribute up to $1,200 ($8,000 × 15%) to an IRA in 1981. For tax years beginning after 1981, an individual whether or not an active participant in a qualified employer plan or in a government plan, may take an income tax deduction for his or her cash contributions to an IRA account each year to the extent of the smaller of the following amounts (a) $2,000 or (b) one hundred per cent (100%) of an individual's annual earned compensation. If A earns $50,000, in 1982, even if he is a participant in an employer qualified plan, $2,000 can be contributed to an IRA. If the maximum $2,000 contribution is made every year to an IRA which earns 8% interest, the account will contain $146,200 at the end of 25 years. If the account continues to earn 8% interest, over $13,000 per year can be withdrawn for 25 years before the funds will be exhausted.

Under both types of individual plans, there is 100% vesting immediately,[55] but the proceeds must begin to be withdrawn when the owner is between the ages of 59½ and 70½ unless the owner is disabled or dies prior to reaching age

59½.[56] Furthermore, both plans allow the naming of a beneficiary to receive the proceeds of the plan at the employee's death.[57] All amounts distributed from an IRA are taxable to the recipient in the year received as ordinary income with no part being eligible for capital gain treatment.[58] A portion of the proceeds from a Keogh plan may, however, be entitled to capital gains treatment in the same manner as the proceeds from corporate plans.[59]

The owner of a qualified retirement plan can name a trust as the beneficiary of the proceeds of the plan. A child of the plan's owner can, in turn, be designated as the beneficiary of the trust. By designating a trust as the beneficiary of the retirement plan, probate is avoided and an orderly manner for distributing the trust assets for the child's benefits can be stipulated in the trust instrument. Furthermore, the benefits from the qualified plan will not be includable in the employee's estate as the proceeds are not paid to the estate.[60]

FOOTNOTES

[1] C. Sternhell & W. Shur, *Probability, Mortality, and Money Concepts,* in Life and Health Insurance Handbook 134 (1973). The length of the payments is governed by the life of the annuitant. E. Vaughn & C. Elliott, Fundamentals of Risk and Insurance 179 (2nd ed. 1978).

[2] R. Mehr, *Contracts-Annuities,* in Life and Health Insurance Handbook 88 (1973).

[3] S. Foosaner, Taxation of Life Insurance and Annuities § 3.01 (1960).

[4] H. Weinstock, Planning an Estate § 11.1 (1977).

[5] *Id.* at § 11.12.

[6] *See generally H. Weinstock, supra* note 4 at §§ 11.3-.6 (1977).

[7] *H. Weinstock, supra* note 4 at § 11.3 (1977). A straight life annuity is usually used in group annuities rather than individual annuities. R. Mehr, *Contracts-Annuities,* in Life and Health Insurance Handbook 83 (1973).

[8] R. Mehr, *Contracts-Annuities,* in Life and Health Insurance Handbook 83 (1973). There are two factors to consider in determining whether to purchase a straight life annuity or an annuity which promises a minimum total return. These factors are the annuitant's age at the time the payments are to begin and the necessity to provide income for dependents if the annuitant dies early. *Id.* at 84.

[9] *Id.*

[10] *Id.*

[11] *Id.* at 86.

[12] *Id.* at 84.

[13] I.R.C. § 72 (b).

[14] Treas. Reg. § 1.72-5 (1956).

[15] Treas. Reg. § 1.72-5 (1956). *See* Treas. Reg. § 1.72-9 (life expectancy tables).

[16] Treas. Reg. § 25.2512-6 (a) (1958).

[17] The present value is includable even though the taxpayer has actually received nothing and has designated a beneficiary to receive the annuity at the taxpayer's death. I.R.C. § 2039 (a).

[18] *Id.* Death benefits paid to an employee's surviving spouse pursuant to an employment contract are not includable in the employee's estate. [1972] 2 Fed. Est. & Gift Tax Rep. (CCH)¶ 6880.056.

[19] Treas. Reg. § 20.2039-1 (a). The total present value is includable if the entire cost of the annuity is paid by the taxpayer or by the employer due to the taxpayer's employment. The fractional part of the cost of the annuity not paid by the employer due to the taxpayer's employment is not includable. A payment is made due to the taxpayer's employment if made as an inducement to employment or in place of added compensation. Treas. Reg. § 20.2039-1 (c). The estate of the annuitant incurs no estate tax liability for a straight life annuity because the annuity terminates at the death of the annuitant and therefore has no present value. *H. Weinstock, supra* note 4 at § 11.10 (1977).

[20] *See* Treas. Reg. § 20.2031-10 (1970). Table A(1) applies to life annuities for males, Table A (2) to life annuities for females, and Table 3 to all term annuities. These tables are computed on the basis of a 6 percent per year interest rate compounded annually.

[21] I.R.C. § 2039 (c).

[22] I.R.C. § 401 (a) (13).

[23] I.R.C. § 2039 (c). To be excluded from the employee's estate under I.R.C. § 2039 (e), the payments must be made over a minimum of 36 months following the employee's date of death. The periodic payments must also be substantially equal. I.R.C. § 2039 (e).

[24] I.R.C. § 501 (a).

[25] For a detailed discussion of all qualified retirement plans, *see* I.R.C. § 401-415. A tax-sheltered annuity is a fifty type of annuity. This type of annuity allows employees of educational institutions and certain other institutions designated in I.R.C. § 501 (c) (3) to have up to 20% of their salary withheld and contributed to an annuity. The amount withheld is treated as an employer contribution and is therefore not taxable to the employee. For a further discussion of the rules applicable to tax-sheltered annuities, *see* I.R.C. § 403 (b).

[26] A defined contribution plan normally consists of a profit sharing plan or a money purchase pension plan or a combination of both. A profit sharing plan allows employees to participate in their employer's profits. A money purchase pension plan pays benefits to the employees or their beneficiaries after retirement without regard to the employer's profits. Treas. Reg. § 1.401-1 (a) (2).

[27] I.R.C. § 401 (j) (1). A combination of these plans can also be used. *Id.*

[28] The contribution to a profit-sharing plan is limited to 15% of the employee's annual compensation. I.R.C. § 404 (a) (3) (A). The maximum dollar amount that may be contributed annually to a defined contribution plan for any single employee is $41,500 per year beginning January 1, 1981. I.R. 81-16 (1981). This amount is periodically adjusted to reflect increases in the cost of living. Treas. Reg. § 1.415-5 (a). Neither a defined contribution plan nor a defined benefit plan can discriminate in favor of officers, shareholders or highly compensated employees. I.R.C. § 401 (a) (4). In order for a defined contribution plan to be nondiscriminatory, the same percentage of each participant's annual salary must be contributed to the plan. Under a defined benefit plan all employees receiving the same salary and/or with the same years of service must be promised the same benefits. Treas. Reg. § 1.401-4 (1956). For example, a covered employee may be provided with a retirement benefit equal to 1 percent of his annual compensation for each year of service. If the employee has an average annual salary of $10,000 and has been covered by the plan for 25 years, his retirement benefit will be $2,500 per year (25% of $10,000).

[29] I.R.C. § 414 (i).

[30] The proceeds from defined contribution and defined benefit plans do not have to be withdrawn between specified ages. Treas. Reg. § 1.401 (a) - 14 (a) (1976). The amount available to the employee on retirement is based on the investment success of the plan. I.R.C. § 414 (i).

[31] A corporate plan may require an employee to be employed for a specified period of time before being able to withdraw the total proceeds from the plan. If there is no such length of time requirement, the employee is said to be 100% vested. If there is a length of employment requirement, the employee is initially eligible to withdraw only a percentage of the proceeds of the plan. This percentage increases in a manner set forth in the vesting schedule of the plan until the employee is 100% vested. For a detailed analysis of all rules concerning vesting requirements, *see* I.R.C. § 411.

[32] I.R.C. §§ 414 (j), 415 (b). Beginning January 1, 1981, the maximum annual benefit that can be promised under a defined benefit plan is $124,500. I.R.-81-16 (1981). This amount is periodically adjusted to reflect increases in the cost of living. Treas. Reg. § 1.415-5 (a).

[33] I.R.C. § 415 (b). The four fundamental types of defined benefit formulas are: (1) flat amount, (2) flat percentage of earnings, (3) flat amount per year of service, and (4) percentage of earnings per year of service. Under a flat amount formula, each employee is entitled to a set retirement benefit, for example, $1,000 per year, regardless of length of service or earnings. A flat percentage earnings formula provides an employee with a benefit equal to a specified percentage of either career average or final average earnings. For example, a plan providing a retirement benefit of 20% of final average earnings will provide $2,000 per year to an employee whose final average earnings are $10,000 per year. A flat amount per year of service formula provides a specified amount of retirement income for each year of an employee's service. For example, a plan providing $50 per year of service provides a retirement benefit of $1,000 per year ($50 x 20 years) to an employee with 20 years of service. Under a percentage of earnings per year of service formula, an employee's yearly retirement benefit is equal to a specified percentage of the employee's earnings for each year of participation in the plan. For example, a plan provides a benefit of 1% of each employee's yearly earnings and participating employee, A, has annual earnings of $10,000, $15,000 and $20,000 for his 3 years of service. A would be entitled to a retirement benefit of $450 per year (1% of $10,000 + 1% of $15,000 + 1% of $20,000). *See* E. Allen, ***Pension Plan Design and Funding Considerations,*** in Life and Health Insurance Handbook 535 (1973).

[34] I.R.C. § 404 (a).

[35] Treas. Reg. §§ 1.402 (a)-1 (a) (i) (1956), 1.403 (a)-1 (a) (1956).

[36] *See* note 23 and accompanying text *supra.*

[37] Gift tax is payable on the portion of the annuity attributable to contributions made by the employee. I.R.C. § 2517. Payments from a qualified plan, made to the participating employee's beneficiary, are taxable to the beneficiary under the same rules that apply to taxation of payments made to the employee. Treas. Reg. § 1.403 (a)-1 (c) (1956). For a further discussion of the applicable rules, *see* notes 45 & 46 and accompanying text *infra.*

[38] I.R.C. § 402.

[39] Treas. Reg. § 1.402 (a)-1 (1956).

[40] *Id.* For a discussion of the amount of an annuity payment that is subject to tax as ordinary income, *see* notes 13 through 15 and accompanying text *supra.*

[41] For a further explanation of the exclusion ratio, *see* notes 13 through 15 and accompanying text *supra.*

[42] I.R.C. § 72 (d) (1).

[43] The lump-sum distribution must include the entire amount to the employee's credit in the plan and must be taken within one taxable year. Furthermore, the lump-sum must be distributed after the employee reaches age 59½ unless he dies or his employment is terminated prior to his reaching age 59½. I.R.C. § 402 (e) (4).

[44] The taxable portion of the distribution which is attributable to the employee's participation in the plan prior to 1974 may be treated as long-term capital gain. I.R.C. § 402 (a) (2). If treatment of the pre-1974 participation as capital gain is not advantageous due to the minimum tax, the entire distribution can be treated as ordinary income. I.R.C. § 402 (e) (4) (L).

[45] The taxable part of the distribution which is attributable to participation after 1973 is treated as ordinary income, I.R.C. § 402 (a) (2).

[46] For example, the recipient of a lump-sum distribution may be entitled to use the ten-year averaging rule, I.R.C. § 402 (e) (1) (C), or may be subject to the six-year "look-back" rule, I.R.C. § 402 (e) (2).

[47] H. Weinstock, *supra* note 4 at §§ 13.18,.19 (1977).

[48] A self-employed person is one who owns more than 10% of a partnership. I.R.C. § 401 (c) (3). A Keogh plan must benefit all employees with 3 or more years of service with the company. I.R.C. § 401 (d) (3), and cannot discriminate in favor of officers, supervisory personnel or highly paid employees. Treas. Reg. § 1.401-12(e) (1963).

[49] I.R.C. § 404 (e) (1). This is the maximum amount that is deductible for contributions to the plan. *Id.*

[50] *Id.*

[51] Below is a table showing what an annual investment of $1 for specified time periods will be worth if 8% interest is earned. To find the amount available, multiply the annual amount to be invested times the appropriate figure. For example, if $1,000 is to be invested each year for 20 years at 8% interest, $45,760 ($1,000 x 45.76) will be available as a retirement fund at the end of the 20 year period.

Years	8%
5	5.86
10	14.48
15	27.15
20	45.76
25	73.10
30	113.28

[52] Below is a table which shows the amount required so that specified amounts can be withdrawn annually, leaving a balance of zero at the end of 25 years. While there are no further contributions after the withdrawals begin, the fund is presumed to earn 8% interest. For example, if an annual income of $20,000 per year is desired, a fund of $213,500 is required. At the end of 25 years, the fund will have a zero balance.

Annual Withdrawal	Fund Invested at 8% Annually
$10,000	$106,750
12,000	128,100
14,000	149,450
16,000	170,800
18,000	192,150
20,000	213,500
22,000	234.850
24,000	256,200
26,000	277,550
28,000	298,900

[53] I.R.C. § 219 (b) (2).

[54] I.R.C. § 219 (b) (1).

[55] I.R.C. § 401 (d) (2) (A) (Keogh vesting requirement); I.R.C. § 408 (a) (4) (I.R.A. vesting requirement).

[56] Treas. Reg. § 1.401-12 (M) (1963) (Keogh pay-out rules).

[57] I.R.C. § 401 (d) (7) (payment to beneficiaries of Keogh accounts); I.R.C. § 408 (a) (payment to beneficiaries of individual retirement accounts).

[58] I.R.C. § 408 (1).

[59] A self-employed participant in a Keogh plan can elect to treat pre-1974 participation a capital gain in the same manner as a participant in a corporate plan. Treas. Reg. § 1.402 (a) -1 (a) (1956). *See* notes 44 & 45 and accompanying text *supra*. The lump-sum distribution must be made after the self-employed participant reaches age 59½ unless he dies or is disabled prior to reaching age 59½ I.R.C. § 402 (e) (4).

[60] H. Weinstock, *supra* note 4 at §§ 3.17, 6.31 (1977).

CHAPTER NINE
GENERATION-SKIPPING TRANSFERS

A generation-skipping transfer generally involves a trust, or similar arrangement,[1] which splits benefits between at least two generations of beneficiaries who are younger than the grantor or creator of the trust.[2] Any reference in this chapter to a generation-skipping trust shall be treated as including generation-skipping trust equivalents, such as life estate and remainder interests.[3] Prior to 1976, generation-skipping transfers were used to defer the imposition of estate and gift taxes for long periods of time.

For example, property placed in trust, to pay income to the grantor's child for his lifetime, and upon the child's death, income to a grandchild for his lifetime, with the property vesting in a great-grandchild at the grandchild's death, would not be subject to tax either in the child's or the grandchild's estate. Estate tax would be imposed only upon the death of the grantor and great-grandchild, which could be more than 100 years apart. The generation-skipping transfer tax, passed by Congress in 1976, now causes these transfers which "skip" generations to be much less attractive as a means of avoiding estate taxes, by imposing a generation-skipping transfer tax.

GENERAL RULES

In order to determine if a generation-skipping transfer exists, the statute provides a method of assigning beneficiaries to generations. For related persons, this method requires generations to be determined along family lines.[4] Where generation-skipping transfers are made to persons outside the family, generations are considered to be in segments of 25 years with the first generation beginning 12½ years after the grantor's birth.[5] A younger generation beneficiary is any beneficiary who is assigned to a generation younger than that of the grantor.[6]

The "grantor" is any person contributing to or adding property to the trust. A beneficiary is any person who has a present or future interest, or power in the trust.[7] A person has an interest in a trust if he has a right to receive income or corpus from the trust or if he is a permissable recipient of income or corpus.[8] A power includes any power to establish or alter beneficial enjoyment of corpus or income of the trust;[9] however, certain powers are not taken into account in determining if a person is a beneficiary of the trust, including the power to appoint among the lineal decedents of the grantor and limited powers held by an independent trustee.[10]

Identifying a trust as a generation-skipping trust requires analysis of the relationship of the beneficiaries to the grantor and to each other. This initial question is illustrated by the following examples:

> Example 1:
> Grantor creates a trust with income payable to his daughter for life, remainder to his granddaughter. This is a generation-skipping trust, since it splits benefits between at least two generations of beneficiaries that are both younger than that of the grantor; however, all or part of the trust may be covered by a special exemption from the generation-skipping transfer tax, applicable to transfers vesting property in grandchildren and described later in this chapter.
>
> Example 2:
> Grantor creates a trust with income payable to grandchild A for life, remainder to grandchild B. This is not a generation-skipping trust. Even though both beneficiaries belong to a younger generation than that of the grantor, both beneficiaries belong to the same generation.

Example 3:
Grantor creates a trust with income payable to his wife for life, remainder to his children. This is not a generation-skipping trust since the benefits are not split between two younger generations. The wife is treated as a member of the same generation as the grantor, regardless of her age.

For generation-skipping transfer tax purposes, a tax is not imposed when the generation-skipping trust is created. Instead, the tax on the generation-skipping transfer will be imposed upon the ocurrence of either a taxable distribution or a taxable termination. A taxable distribution is any distribution, payable out of amounts other than current trust income, to a younger generation beneficiary assigned to a generation younger than the generation assignment of any other younger generation beneficiary (See Example 4 below). A taxable termination is the termination (by death, lapse of time, exercise or nonexercise, or otherwise) of the interest or power in a generation-skipping trust of any younger generation beneficiary assigned to a generation older than the generation assignment of any other younger generation beneficiary. (See example 5 below)[12] Thus, the generation-skipping tax will not be imposed until a generation-skipping transfer occurs.

Example 4:
Grantor creates a trust with income payable to his grandson S for life, remainder to S's daughter D. The trustee has discretion to make distributions from corpus to S's daughter D, while S is still alive. This is a generation-skipping trust since the trust splits the benefits between at least two generations of beneficiaries that are younger than that of the grantor, and the trust has younger generation beneficiaries assigned to more than one generation. Any distribution of corpus to S's daughter D while S is alive will result in a taxable distribution. A distribution of current trust income to D, or a distribution of corpus or current income to S will not result in a taxable distribution.

> Example 5:
> Grantor creates a trust with income to grandson S for life, remainder to S's daughter D. This is a generation-skipping trust for the same reasons discussed in example 4. No generation-skipping tax will be levied upon this trust until the death of S, when a taxable termination of his life interest occurs.

EXCEPTIONS

Several exceptions and limitations on the rules relating to taxable distributions and taxable terminations may prevent application of the generation-skipping transfer tax. The first exception exempts generation-skipping transfers that are also subject to either estate or gift tax.[13]

> Example 6:
> Grantor creates a trust with income to his grandson B for life, remainder to B's children. Grantor also grants to B a general power of appointment over the trust. Assuming B does not exercise his general power, the trust will be taxable in B's gross estate for estate tax purposes;[14] therefore, no taxable termination will be deemed to occur at B's death.

A second exemption applies to any generation-skipping transfer to the extent property is transferred to grandchildren of the grantor of the trust, but only to the extent that such transfers with respect to any deemed transferor (defined later in this chapter) do not exceed $250,000 in value.[15]

> Example 7:
> Grantor creates a trust with income to daughter D for life, remainder to D's children. D will be the deemed transferor. If D dies, survived by four children who receive the trust corpus of $1 million equally, a taxable termination of $750,000 (the excess of the trust property over $250,000) will occur upon D's death (assuming no prior generation-skipping transfers).

> Example 8:
> Grantor creates two trusts: Trust A to pay income to his son X for life, remainder to X's son S, Trust B to pay income to his daughter Y for life, remainder to Y's daughter D. Each trust has available an exclusion of $250,000 (assuming no prior generation-skipping transfers), so that property having a value of up to $500,000 may pass to grandchildren S & D free of the generation-skipping transfer tax.

A third exception to the taxable distribution and termination rules states that an individual who at no time has any interest other than a future interest or future power (or both) in the generation-skipping trust, shall not be considered a younger generation beneficiary.[16] A fourth exception provides that a taxable termination will be postponed if any one of four special postponement rules apply.[17] A fifth exception prevents the generation-skipping tax from being imposed more than once on each generation.[18]

COMPUTATION OF THE TAX

After a taxable distribution or termination has been made, the generation-skipping tax due is computed by determining the value of the property transferred, its tax base, the allowable deduction, the applicable tax rate and the available credits against the tax.

The tax base for a taxable distribution is the fair market value of the property distributed to a younger generation beneficiary, determined as of the date of distribution.[19] The tax base for a taxable termination is the fair market value of the trust property in which an interest or power has terminated, determined as of the date of termination.[20] If a transfer is both a taxable distribution and termination, the taxable termination rules apply.[21]

The tax base is reduced by certain deductions, including charitable deductions[22] and deductions for certain expenses, indebtedness, taxes, or losses incurred by the generation-skipping transfer.[23] These deductions will vary according to the type of taxable event and the time of that event. The net generation-skipping transfer is subject to the generation-skipping transfer tax. The same unified tax rate schedule applicable for determining estate and gift taxes is utilized for computing the tax on generation-skipping transfers.[24] The applicable tax rate is determined not by reference to the transferor or grantor of the trust but rather by reference to the deemed transferor.

The deemed transferor will generally be the parent of the transferee (the one to whom the property is passing) who is more closely related to the grantor of the trust. If neither parent is related to the grantor, the parent having the closest affinity to the grantor will be the deemed transferor.[26] If, however, that parent is not a younger generation beneficiary of the trust, but one or more ancestors of the transferee is a younger generation beneficiary related by blood or adoption to the grantor of the trust, the youngest of such ancestors will be the deemed transferor.[27]

After the deemed transferor is determined, the tax imposed on the generation-skipping transfer is the excess of:

1. A tentative tax computed under the unified rate tables in Section 2001 (c) (as in effect on the date of the transfer) on the sum of:

   a. The fair market value of the generation-skipping property transferred on the date of the transfer;

   b. The aggregate fair market value of all prior generation-skipping transfers of the deemed transferor;

   c. The amount of taxable gifts made after December 31, 1976, but before the current transfer, by the deemed transferor (not included are gifts taxable in his gross estate for estate tax purposes), and;

d. If the deemed transferor died at the same time as, or before, the current transfer, the taxable estate of the deemed transferor; over

2. A tentative tax on the sum of the amounts determined under items "b" through "d" above.[28]

Example 9:
Grantor creates a trust with income to his grandson B for life, remainder to B's son S. The trustee has the power, in his discretion to make distributions of corpus to B's son S during B's lifetime. Assuming that, since December 31, 1976, B has made taxable gifts of $2 million, B's taxable estate at his death is $3 million, the Trustee has made previous discretionary distributions of trust corpus to B's son amounting to $1 million, and the trust corpus is worth $4 million at the time of B's death, the generation-skipping transfer tax imposed upon the termination of B's life interest in the trust will be computed in the following manner:

Current generation-skipping transfer (trust corpus)	$ 4,000,000
Prior generation-skipping transfers attributed to B (distributions to B's son S)	$ 1,000,000
Taxable gifts made by B	$ 2,000,000
Taxable estate of B (since he died at the same time as the taxable termination)	$ 3,000,000
Total	$10,000,000
Tentative tax on $10,000,000 under unified rate tables[29] (as in effect for 1981)	$ 6,050,800
Less:	
Tentative tax on $6,000,000 (amount of prior transfers, taxable gifts, and taxable estate of B)	$ 3,250,800
Generation-skipping transfer tax (gross amount)	$ 2,800,000

If the generation-skipping transfer of $4,000,000 had been taxed separately under the unified rate schedule (as in effect for 1981), the tax would be $1,880,800. By combining the generation-skipping transfer with all other transfers of the deemed transferror, the generation-skipping tax is increased by $919,200.

The tax on the generation-skipping transfer may be reduced by any one or more of three allowable credits. If the generation-skipping transfer occurs at the same time as, or after, the death of the deemed transferor, then the unused portion of the unified credit may offset the generation-skipping tax.[30] In addition, a credit for tax on prior transfers may be available against the generation-skipping tax.[31] Finally, if the generation- skipping transfer occurs at the same time as, or after, the death of the deemed transferor, an amount equal to that portion of the estate, inheritance, legacy, or succession tax actually paid to a state in respect of any property included in the generation-skipping transfer may also offset the generation-skipping tax.[32] Liability for the generation-skipping tax falls on the trust. If the trust fails to pay the generation-skipping tax, the trustee is liable for the tax due if it results from a taxable termination,[33] and the distributee (the person receiving the distribution) is liable for the tax due if it results from a taxable distribution.[34] Each distributee is liable for his pro rata share of taxes due if more than one person receives property as a result of a taxable distribution.

The person required to file the return, with respect to generation-skipping taxes is, in the case of a taxable distribution, the distributee, or in the case of a taxable termination, the trustee.[35] The return is to be filed and the tax paid on or before the 90th day after the close of the taxable year of the trust in which such transfers occurred if the generation-skipping transfer occurred while the deemed transferor was alive.[36] In the case of a generation-skipping transfer occurring at the same time as, or after, the death of the deemed transferor, the return is to be filed and the tax paid within ninety days of the last day allowed for filing the deemed transferor's estate tax return, or, if later, within nine months after the day on which such generation-skipping transfer occurred.[37]

FOOTNOTES

[1] I.R.C. § 2611 (d)

[2] *Id.*

[3] *Id.*

[4] I.R.C. § 2611 (c) (1)

[5] I.R.C. § 2611 (c) (5)

[6] I.R.C. § 2613 (c) (1)

[7] I.R.C. § 2613 (c) (3)

[8] I.R.C. § 2613 (d) (1)

[9] I.R.C. § 2613 (d) (3)

[10] I.R.C. § 2613 (e)

[11] I.R.C. § 2613 (a) (1)

[12] I.R.C. § 2613 (b) (1)

[13] I.R.C. § 2613 (a) (4) (B), 2613 (b) (5) (B)

[14] I.R.C. § 2041

[15] I.R.C. § 2613 (A) (4) (A), 2613 (b) (5) (A), 2613 (b) (6)

[16] I.R.C. § 2613 (a) (1), 2613 (b) (1)

[17] I.R.C. § 2613 (b) (2) (A-D)

[18] I.R.C. § 2613 (b) (7) (B)

[19] I.R.C. § 2602 (a) (A)

[20] I.R.C. § 2602 (a) (1) (A)

[21] I.R.C. § 2613 (b) (7) (A)

[22] I.R.C. § 2602 (c) (2)

[23] I.R.C. § 2062 (c) (5) (B)

[24] I.R.C. § 2602 (a) 2001 (c), 2502 (a)

[25] I.R.C. § 2612 (a)

[26] I.R.C. § 2612 (a) (1)

[27] I.R.C. § 2612 (a) (2)

[28] I.R.C. § 2602 (a)

[29] I.R.C. § 2001 (c)

[30] I.R.C. § 2602 (c) (3)

[31] I.R.C. § 2602 (c) (4)

[32] I.R.C. § 2062 (c) (5) (C)

[33] I.R.C. § 2603 (a) (1) (A)

[34] I.R.C. § 2603 (a) (1) (B), 2603 (a) (3)

[35] I.R.C. § 2621 (c)

[36] *Id.*

[37] *Id.*

APPENDIX A
SAMPLE WILL AND TRUST PROVISIONS

For sample drafting language, the authors refer legal counsel to the *Mississippi Will and Trust Manual*, Don L. Fruge', Mississippi Editor. No will or trust agreement should be executed without competent legal and tax advice by a person licensed to provide such services.

The following provisions not specifically included in the Mississippi Will and Trust Manual may be used with appropriate modification for incorporation into a trust created by a parent for the care of his retarded child, particularly if the parent wishes to limit the invasion of such trust by state institutions seeking reimbursement for costs of care supplied to the child. They are merely suggested, and do not encompass all dispository and administrative procedures that will be needed in such a trust.

1. *Dispository Provision*. As long as my daughter, Jane Doe, does not reside in a state institution or retardation center, the trustee shall pay or apply as much of the net income and principal of the trust as the trustee in his sole discretion determines necessary for the care, support, maintenance, and education of my daughter, after taking into account all other income and resources of my daughter including public financial assistance. If my daughter at any time during her lifetime becomes a resident of a state institution or retardation center, the trustee shall accumulate the net income of the trust, and such accumulated income shall be added to principal of the trust; and the trustee shall apply as much of the principal of the trust as the trustee in his sole discretion determines necessary to provide my daughter with goods and services of a kind not provided by the state institution or retardation center at which she resides, or by government

financial assistance benefits [specifically enumerate the goods and services to be covered, such as health and medical services not provided, entertainment, clothing, travel and transportation, etc.].

2. *Grantor's Intent.* It is the grantor's intent that the funds of this trust be used only to supplement benefits available to the beneficiary through government financial assistance benefits and institutional care and support and to provide for items not available to the beneficiary through this assistance; and the provisions of this trust shall be construed in a manner consistent with this intent.

3. *Instruction to Trustee.* The trustee is directed to apply for and collect for the trust beneficiary any government financial assistance for which the beneficiary qualifies. Said benefits shall not be commingled with this trust fund, and shall be expended prior to invasion of this trust by the trustee as provided under Paragraph 1.

4. *Spendthrift Provision.* No part of any trust under this will, principal, income or increment thereof shall be attachable, assignable, trustable or liable to be taken at law or in equity for or on account of any debt, obligation or contract of any beneficiary hereunder, including amounts owed to federal, state, or local governments and other providers of services of financial assistance to the beneficiary, or claims for support of any person including the state government or its political subdivisions.

5. *Termination Clause.* If a decision is rendered by a court of competent jurisdiction that the interest of my daughter in this trust, as set forth under Paragraph 1, renders her ineligible for Supplemental Social Security, Medicaid, or other similar benefits provided through government assistance, or that the trust is subject to attachment, assignment, or

execution by a creditor (including a provider of services) of my daughter, the trustee may terminate this trust. Upon termination, pursuant to this provision, the principal and any accrued income thereon shall be distributed to my then surviving issue (other than my daughter, Jane Doe) per stirpes.

APPENDIX B

*RESOURCE GUIDE FOR FURTHER READING

1. Estate Planning

Casner, A. James. *Estate Planning*, 1979.

Doyle, Phillis B., et al. *Helping the Severely Handicapped Child: A Guide for Parents and Teachers.* Thomas Y. Crowell, Publishers, 10 East 53rd Street, New York, New York 10022, 1979.

Estate Planning and Drafting Techniques. Thirty-Third Annual Mississippi Law Institute, 1978.

Frolik, Lawrence A. "Estate Planning for Parents of Mentally Disabled Children." *University of Pittsburgh Law Review,* V 40 N 3, Spring, 1979, 305-326.

Fruge', Don L. Editor. *Mississippi Will and Trust Manual,* 1979 (with annual supplement).

How to Provide for Their Future. National Association for Retarded Children, 420 Lexington Avenue, New York, New York 10017, 1978.

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Rabkin and Johnson, *Current Legal Forms with Tax Analysis,* 1981 (with annual supplements).

Stephens, Maxfield and Lind. *Federal Estate and Gift Taxation,* 1978.

Streng, William P. Estates, Gifts and Trusts—Planning, 11-8th Tax Management Portfolio, 1979 (with supplements).

II. Guardianship

Appelberg, Esther. "The Significance of Personal Guardianship for Children in Casework." *Child Welfare,* v 49 n 1, January 1970, 6-17.

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Guardianship of Mentally Retarded Persons. New York State Association for Retarded Children, Inc., 175 Fifth Avenue, New York, New York 10010, 1972.

Kock, Richard, and Kock, Kathryn Jean. *Understanding the Mentally Retarded Child: A New Approach*. Random House, 201 East 50th Street, New York, New York 10022, 1974.

McLaughlin, Paul. *Guardianship of the Person*. Canadian Association for the Mentally Retarded, 4700 Keele Street, Downview Ontario M3J 1P3, 1979.

III. Mentally Retarded and the Law

Friedman, Paul R. *The Rights of Mentally Retarded Persons: The Basic ACLU Guide to a Mentally Retarded Person's Rights*. American Civil Liberties Union, 22 East 40th Street, New York, New York 10016. Also available through: Avon Books, Mail Order Department, 250 West 55th Street, New York, New York 10019, 1976.

Herr, Stanley S. *The New Clients: Legal Services for Mentally Retarded Persons*. National Legal Services Corporation. Research Institute on Legal Assistance, 733 Fifteenth Street, N.W., Washington, D.C. 20005, 1979.

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Mann, James W. and Parker, G. Legal Status of the Mentally Retarded and Mentally Ill in Mississippi. *Mississippi Law Journal*, 1969, 91, 78-111.

McLaughlin, Paul. *Estate Planning for the Parents of Mentally Retarded Persons*. Canadian Association for the Mentally Retarded, 4700 Keele Street, Downview Ontario M3J 1P3, 1977.

Mental Retardation-The Law-Guardianship. National Institute on Mental Retardation, 4700 Keele Street, Downview, Ontario, Canada M3J 1P3, 1972.

Smoker, Marliene. *Legal Rights of the Mentally Retarded.* Pennsylvania Association for Retarded Children, Pennsylvania, 1974.

Warren, Sue Allen. "Rights of Mentally Retarded Persons: An Official Statement of the American Association on Mental Deficiency." *Mental Retardation,* v 11 n 5, October 1973, 56-8.

IV. Miscellaneous

Helsel, Elise D., and Graham, Earl C., editors. *Tomorrow is Today - Planning Ahead for Long-Term Care Legally and Financially.* United Cerebral Palsy Associations, Inc., 321 West 44th Street, New York, New York 10036, 1966.

Schleifer, Maxwell J., ed. "The Name of the Game is Economics." *Exceptional Parent,* v 8 n 6, December 1978, E1-30.

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Wolfensberger, Wolf. *Citizen Advocacy for the Handicapped, Impaired, and Disadvantaged: An Overview.* Superintendent of Documents, U.S. Government Printing Office, Washington, D.C. 20402, 1972.